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Supreme Court, U.S.

FILED

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JOSEPH F. SPANIOL, JR.
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No. _____

IN THE
SUPREME COURT OF THE UNITED STATES

October Term 1986

TROXLER HOSIERY CO., INC.
and GERALD S. SCHAFER, TRUSTEE

Petitioner,
vs.

UNITED STATES OF AMERICA,

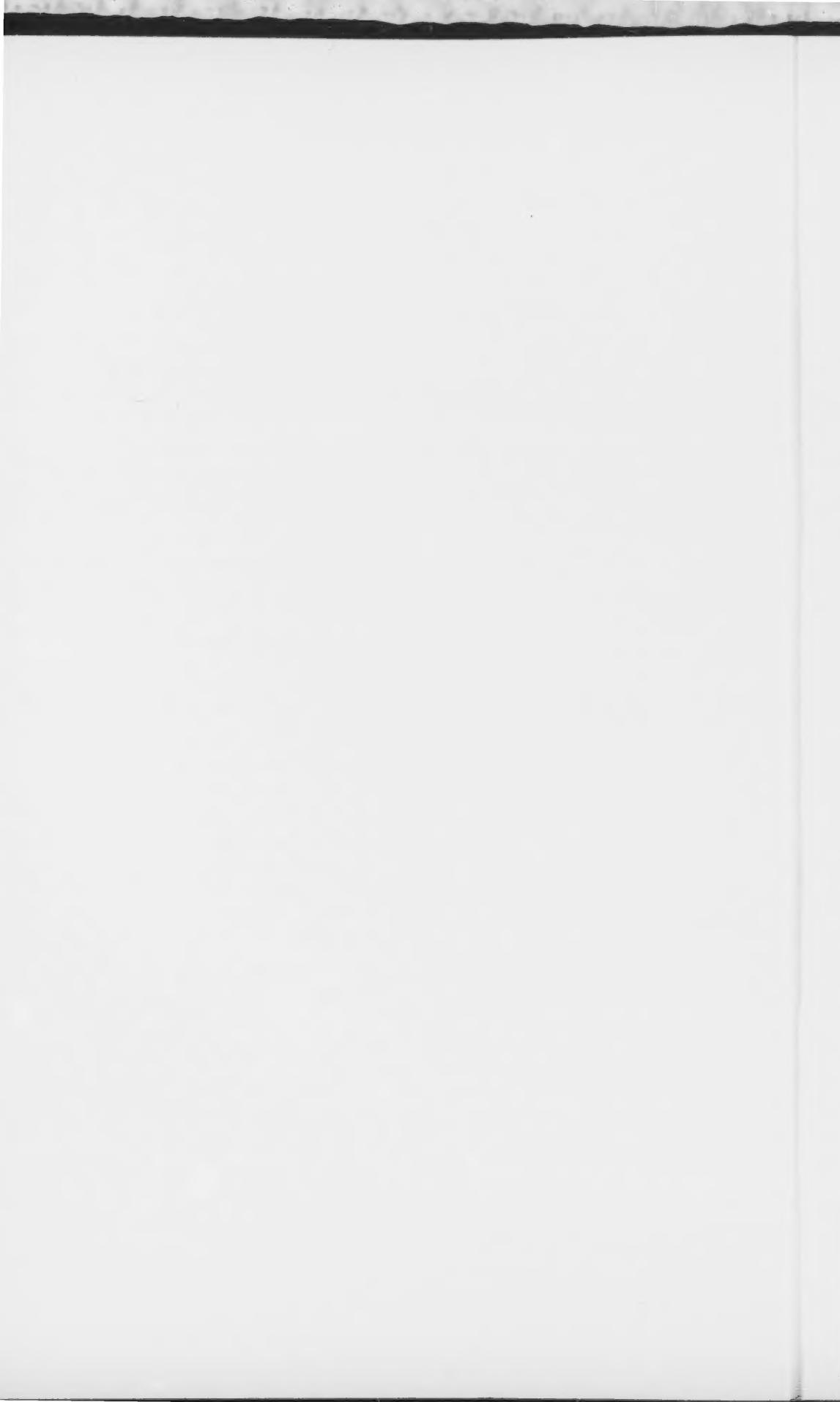
Respondent.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

PETITION FOR CERTIORARI

Charles M. Ivey, III
IVEY, IVEY & DONAHUE
Post Office Box 3324
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Greensboro, North Carolina 27401
Attorney for the Petitioners

1071P



QUESTIONS PRESENTED

I. WHETHER THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT ERRED IN DENYING PETITIONER'S REQUEST FOR REHEARING, PURSUANT TO FEDERAL RULE 40 OF THE FEDERAL RULES OF APPELLATE PROCEDURE AND 28 U.S.C. § 455(a), DESPITE THE FACT THAT TWO FOURTH CIRCUIT JUDGES FAILED TO RECUSE THEMSELVES FROM SITTING ON THE PANEL WHICH AFFIRMED THE ADVERSE DECISION BELOW EVEN THOUGH BOTH JUDGES WERE ON THE PANEL WHICH INITIALLY IMPOSED THE CRIMINAL FINE AGAINST THE PETITIONER?

II. WHETHER THE AUTOMATIC STAY PROVISION OF 11 U.S.C. § 362(a) APPLIES TO THE COLLECTION OF A FINE AND COSTS FOR A CRIMINAL CONTEMPT JUDGMENT?



LIST OF PARTIES INVOLVED

Pursuant to the Rules of this Court, the parties to this proceeding in this Court are as shown in the caption of this Petition for Certiorari.



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OPINIONS BELOW

The Honorable Rufus W. Reynolds, United States Bankruptcy Judge for the Middle District of North Carolina, Greensboro Division, on March 5, 1984, denied the United State's request for a declaratory judgment relieving it from the automatic stay provisions of 11 U.S.C. § 362. Judge Reynolds' Memorandum Opinion is unpublished. A copy of the Opinion and Order are attached hereto in the Appendix. (A)

The Honorable Hiram H. Ward, Chief Judge of the United States District Court for the Middle District of North Carolina reversed the Bankruptcy Court's Order in a published decision dated July 27, 1984, on the ground that the automatic stay of 11 U.S.C. § 362 does



not apply to collection of the criminal judgment claim. A copy of Judge Ward's Opinion is attached hereto in the Appendix. (B)

The United States Court of Appeals for the Fourth Circuit affirmed the District Court's reversal of the Bankruptcy Court's Order in a published decision dated August 4, 1986. A copy of the Fourth Circuit Opinion is attached hereto in the Appendix. (C)

On the Appellant's Petition For Rehearing, the Fourth Circuit denied the same in an Order dated September 24, 1986. The Opinion is attached hereto in the Appendix. (D)



JURISDICTION OF
THE UNITED STATES SUPREME COURT

The United States Bankruptcy Court obtained intitial jurisdiction when the United States of America filed a request with the United States Bankruptcy Court for the Middle District of North Carolina, A-83-0510, seeking a declaratory judgment as to the applicability of the automatic stay provision, 11 U.S.C. § 362(a) to the government's collectibility of its criminal contempt fine against the bankruptcy estate of Troxler Hosiery Co., Inc.

This Petition is filed within ninety (90) days of the denial of the rehearing entered in the United States Court of Appeals for the Fourth Circuit



on September 24, 1986, as required by 28 U.S.C. § 2101(c). The request for rehearing was filed due to the adverse decision rendered by the United States Court of Appeals for the Fourth Circuit on August 4, 1986, which Petitioner also seeks to have reviewed. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1) and Sup.Ct.R. 17.1(a) and (c).



CONSTITUTIONAL PROVISIONS AND
STATUTES INVOLVED

1. (11 U.S.C. § 101)

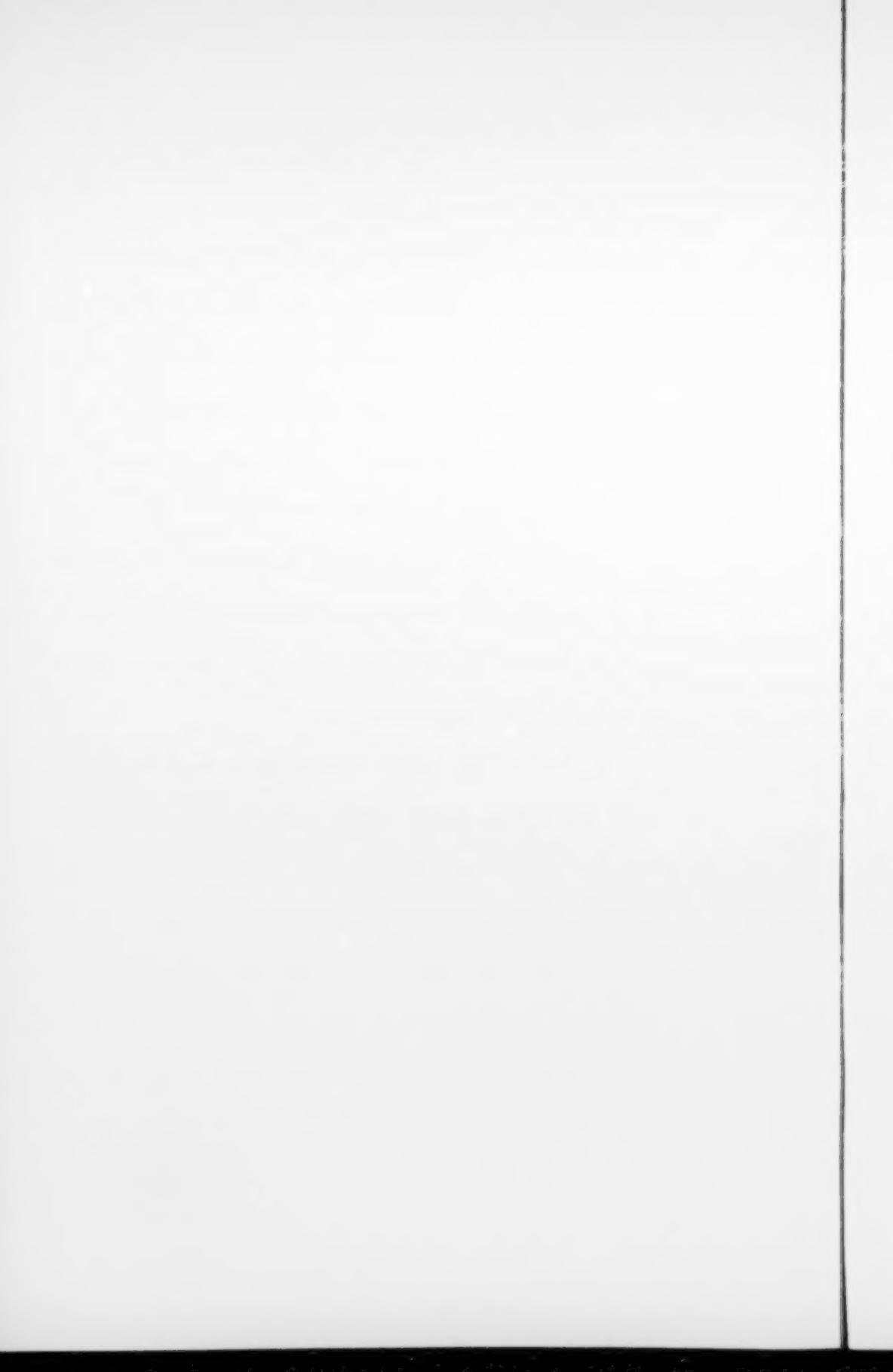
§ 101. Definitions. In this title -

(12) "debtor" means person or municipality concerning which a case under this title has been commenced;

(14) "entity" includes person, estate, trust, and governmental unit;

(21) "foreign representative" means duly selected trustee, administrator, or other representative of an estate in a foreign proceeding;

(33) "person" includes individual, partnership, and corporation, but does not include governmental unit, Provided, however, that any governmental unit that acquires an asset from a person as a result of operation of a loan guarantee agreement, or as receiver or liquidating



agent of a person, will be considered a person for purposes of section 1102 of this title;

2. 11 U.S.C. § 109
(Reproduced in Appendix - E)

3. 11 U.S.C. § 362
(Reproduced in Appendix - F)

4. 11 U.S.C. § 541
(Reproduced in Appendix - G)

5. 11 U.S.C. § 726

(a) Except as provided in section 510 of this title, property of the estate shall be distributed - ...

(4) fourth, in payment of any allowed unsecured claim, whether secured or unsecured, for any fine, penalty, or forfeiture, or for multiple, exemplary, or punitive damages, arising before the earlier of the order for relief or the appointment of a trustee, to the



extent that such fine, penalty, forfeiture, or damages are not compensation for actual pecuniary loss suffered by the holder of such claim;

6. 28 U.S.C. § 455 (a)

(a) Any justice, judge or magistrate of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned.



STATEMENT OF THE CASE

The Petitioner, Troxler Hosiery Co., Inc. (hereinafter referred to as "Troxler") was found in criminal contempt for violating the February 1, 1978, Order of the United States Court of Appeals for the Fourth Circuit, prohibiting the removal of Troxler's Tris-treated goods from the Middle District of North Carolina. After Troxler shipped the Tris-treated goods to Venezuela, contempt proceedings were instituted which culminated on June 21, 1982, in the imposition of an \$82,000.00 fine plus court costs by the Court of Appeals for the Fourth Circuit. United States v. Troxler Hosiery Co., Inc. 672 F.2d 365 (1982).

Troxler filed a voluntary petition



in the United States Bankruptcy Court for the Middle District of North Carolina under Chapter 11 of the United States Bankruptcy Code on November 3, 1982. On February 3, 1983, the United States filed a proof of claim in the bankruptcy proceeding claiming a secured debt in the amount of the fine and the costs. On October 4, 1984, the United States filed an adversary proceeding in the Bankruptcy Court, the court of first instance, which had original jurisdiction and jurisdiction over all related matters since the date of Troxler's petition under Chapter 11, seeking a declaratory judgment that the automatic stay provision of 11 U.S.C. § 362(a) did not apply to stay the collection of the alleged secured debt



arguing that the exception of 11 U.S.C. § 362(b) excepted the collection of the criminal contempt fine from the automatic stay. On March 5, 1984, the Bankruptcy Court denied the government's request, holding that the automatic stay provision of 11 U.S.C. § 362 bars the United States from collecting the judgment. (A) On the 12th day of March, 1984, the Chapter 11 proceeding was converted to a Chapter 7 liquidation proceeding, and Gerald S. Schafer was appointed as the duly qualified and acting Trustee. The appeal to the United States District Court for the Middle District of North Carolina was heard by the Honorable Hiram H. Ward, with arguments being made by counsel to that Court on June 26, 1984. A



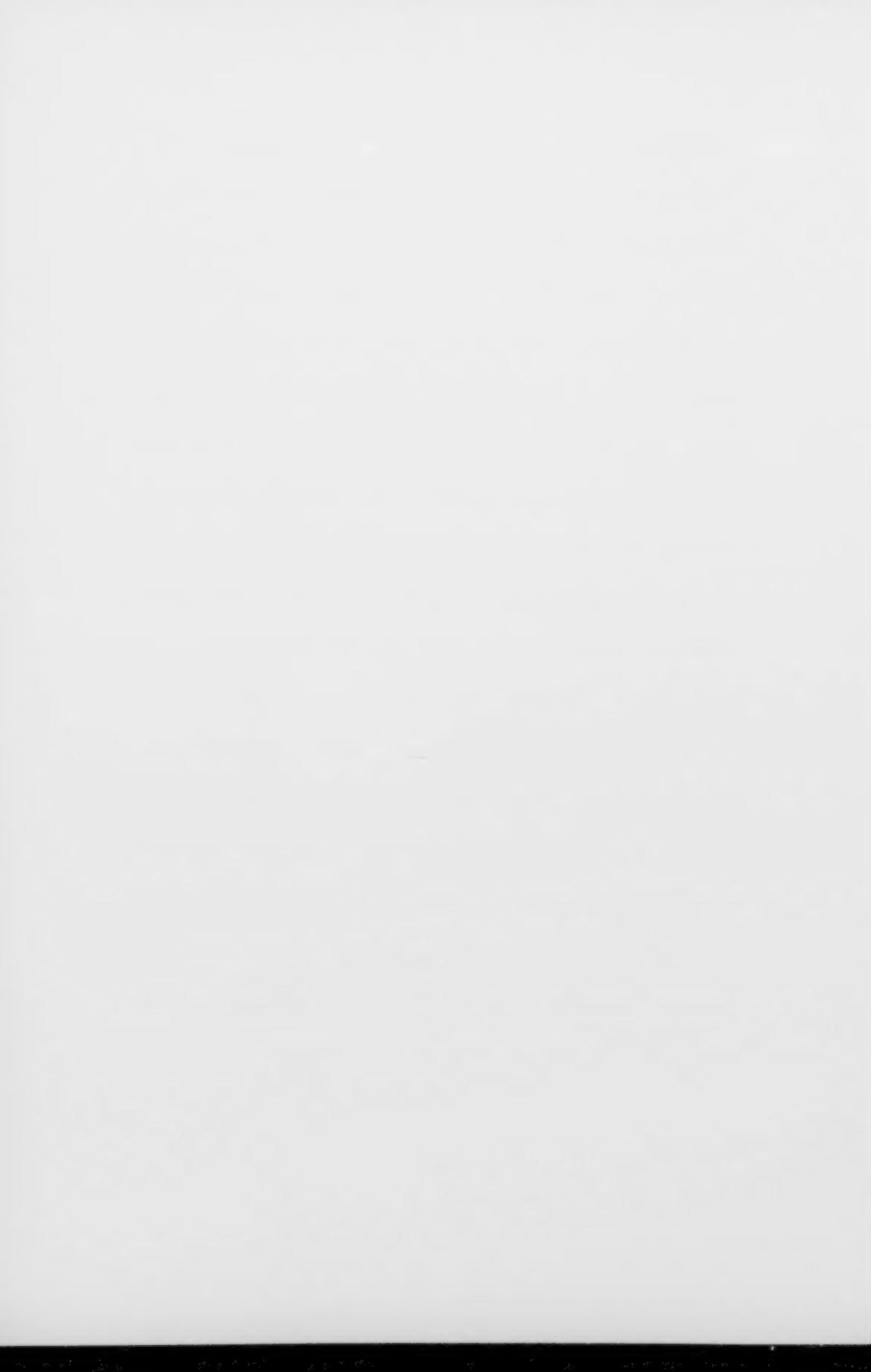
Memorandum Opinion and Order reversing the Honorable Rufus W. Reynolds, United States Bankruptcy Judge, was entered by Judge Ward on June 27, 1984. (B) As a result of that Order, a timely notice of appeal was given by Gerald S. Schafer, the Trustee for Troxler Hosiery Co., Inc., Debtor, to the United States Court of Appeals for the Fourth Circuit.

The Fourth Circuit, in a published decision dated August 4, 1986, per curiam, adopted and affirmed the opinion and order of Judge Hiram Ward. The Court denied the government's motion to supplement the record on appeal to include portions of depositions of Robert Andrew Troxler, Sr. and Robert Andrew Troxler, Jr. (C)

The Petitioner timely filed a



request for a rehearing pursuant to Federal Rule 40 of the Federal Rules of Appellate Procedure and 28 U.S.C. § 455(a) on the bases that the Court overlooked certain material facts and law in making its decision, specifically, refusing to consider the decision rendered by the United States Court of Appeals for the Second Circuit in In Re Robinson, 776 F.2d 30 (2nd Cir. 1985). Additionally, the Petitioner, in the brief filed in support of Petitioner's request for rehearing, challenged the impartiality of two of the Judges affirming the United States District Court's decision in that these two of these Judges were also on the panel which imposed the criminal fine initially.



The Petitioner's request for rehearing was denied on September 24, 1986, by the United States Court of Appeals for the Fourth Circuit. (D)

REASONS FOR GRANTING WRIT

I. WHETHER THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT ERRED IN DENYING PETITIONER'S REQUEST FOR REHEARING, PURSUANT TO FEDERAL RULE 40 OF THE FEDERAL RULES OF APPELLATE PROCEDURE AND 28 U.S.C. § 455(a), DESPITE THE FACT THAT TWO FOURTH CIRCUIT JUDGES FAILED TO RECUSE THEMSELVES FROM SITTING ON THE PANEL WHICH AFFIRMED THE ADVERSE DECISION BELOW EVEN THOUGH BOTH JUDGES WERE ON THE PANEL WHICH INITIALLY IMPOSED THE CRIMINAL FINE AGAINST THE PETITIONER?

The Petitioner respectfully urges the United States Supreme Court to review the merits of this action pursuant to Sup.Ct.R. 17.1(a). The



Fourth Circuit has departed from the accepted and usual course of judicial proceedings by allowing two of the same Judges', which imposed the criminal fine against the Petitioner, to sit on a three-Judge panel to review the collectability of the criminal contempt judgment against the Petitioner.

The decision of the Fourth Circuit three-Judge panel to hear the appeal from the United States District Court which dealt with the enforceability under 11 U.S.C. § 362(b) of a criminal contempt judgment imposed by two members of the Fourth Circuit three-Judge panel departed from the usual and impartial course of judicial proceedings. This substantial departure from the accepted course of judicial dealings, which

insures impartiality and propriety, should be reviewed by this honorable Court, especially in light of 28 U.S.C. § 455(a) which sets forth the accepted course of dealing with issues of impartiality. Applied in, Rice v. McKenzie, 581 F.2d 1114 (4th Cir. 1978).

Once the three-Judge panel, sitting for the Fourth Circuit, imposed a criminal fine upon the Petitioner, See, United States v. Troxler Hosiery Co., Inc., 672 F.2d 365 (4th Cir. 1982), those three Judges were barred, by the requisites of impartiality and 28 U.S.C. § 455(a), from sitting on the Fourth Circuit panel that would decide that same fine's enforceability or collectibility against the Troxler estate. By permitting the two Judges,



who imposed the fine, to sit on the panel which reviewed and affirmed the adverse decision, the Fourth Circuit substantially departed from the accepted and usual course of judicial proceedings in not providing independent federal review for the Petitioner.

II. WHETHER THE AUTOMATIC STAY
PROVISION OF 11 U.S.C. § 362(a) APPLIES
TO THE COLLECTIBILITY OF A FINE AND
COSTS FOR A CRIMINAL CONTEMPT JUDGMENT?

The Petitioner respectfully urges the United States Supreme Court to review the merits of this action pursuant to Sup.Ct.R. 17.1(a) and (c). The Fourth Circuit has decided an important question of federal law, which has not

been, but should be settled by this honorable Court and has decided this important federal question in such a way as to directly conflict with the United States Bankruptcy Code which is a substantial departure from the accepted and usual course of judicial proceedings. This substantial departure significantly adversely affects the day-to-day administration of estates, estates which cannot readily afford to raise such issues on appeal.

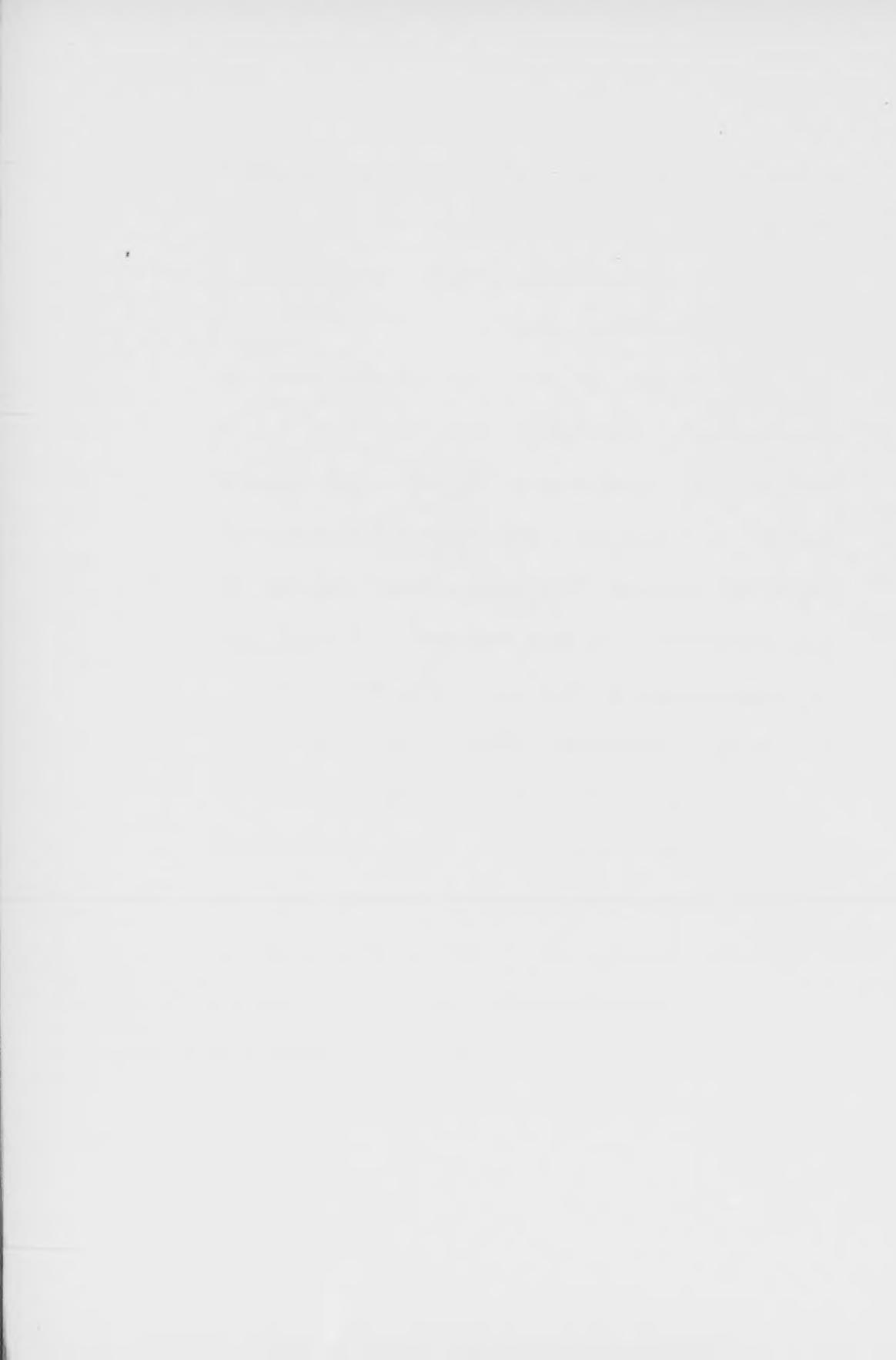
The Troxler case also presents the United States Supreme Court with an important federal question under the United States Bankruptcy Code which has not been but should be settled by this Court: whether the government can collect a contempt fine from a debtor in

bankruptcy regardless of the automatic stay provision of 11 U.S.C. § 362(a) and prior to all other creditors in the estate. The Fourth Circuit decision in Troxler has sanctioned a substantial departure from the accepted and usual course of judicial proceedings, in that the lower Court's decision was decided contrary to the plain meaning of the United States Bankruptcy Code. If this honorable Court does not review the Troxler decision, the government will automatically have status as a judicially created super-priority creditor outside the controls of the Bankruptcy Court and outside the controls of the United States Bankruptcy Code in all bankruptcy proceedings. This judicially created absolute

priority status of the government operates to the impairment of all other creditors in cases where there is a criminal contempt fine.

The scope of the automatic stay in bankruptcy, pursuant to 11 U.S.C. § 362(a), is extremely broad and should apply to almost any type of formal or informal action against the Debtor or the property of the estate. 2 Collier On Bankruptcy § 362.04 (15th Ed. 1983).

The stay "ensures that all of the property of the Debtor may be brought into the custody of the Bankruptcy Court by the filing of a petition, and no interference of that custody can be countenanced without the court's permission ...".



In Re Adana Mortgage Bankers, Inc. 12
B.R. 989 (Bkrtcy. N.D. Ga. 1980).

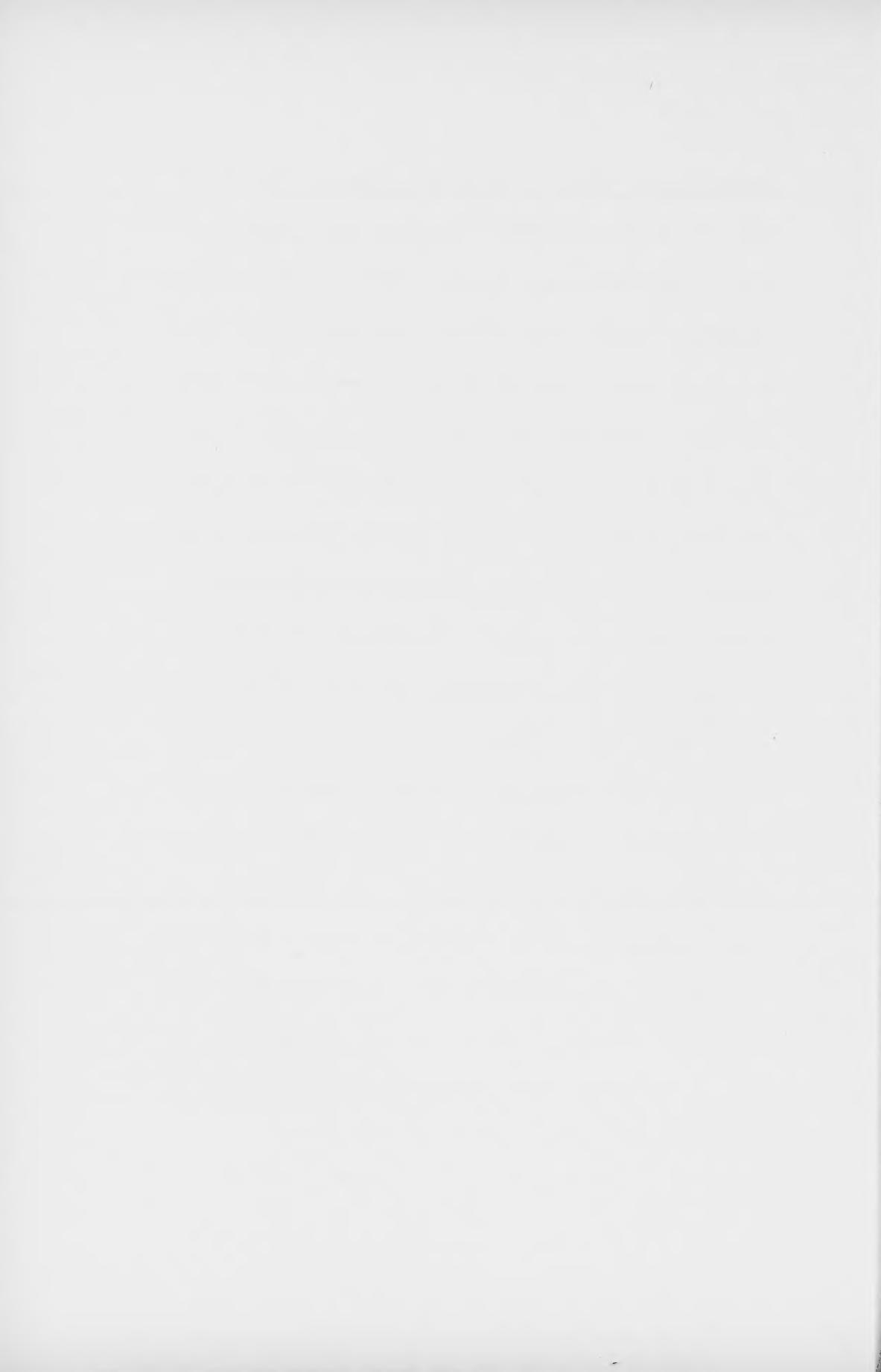
The Section 362 stay operates against most all entities and that term is defined to include government units such as departments, agencies or instrumentalities in the United States. 11 U.S.C. § 101(14), 11 U.S.C. § 101(21). 11 U.S.C. § 362(a) stays the collection of the criminal contempt fine herein unless an exception can be found in 11 U.S.C. § 362(b)(1).

11 U.S.C. § 362(b)(1) specifically excludes the commencement or continuation of a criminal action proceeding and the operation of 11 U.S.C. § 362(a) "against the debtor" and does not apply to actions taken against "property of the estate." In re



Nashville White Truck, Inc., 731 F.2d 376 (6th Cir. 1984); Matter of Gibbs, 9 B.R. 756 (Bkrtcy. D.Ct. 1981). The term "debtor" and the term "property of the estate" are two distinct legal concepts in the context of the Bankruptcy Code. 11 U.S.C. § 541 and 11 U.S.C. § 109. Proceedings against property rather than against the debtor were not intended to come within the Section 362(b)(1) exception. In re Ryan, 15 B.R. 514, 519 (Bkrtcy.D.Md. 1981).

In the Troxler case, however, the government sought to collect its fine through seizure and sale of property of the estate, not against the debtor, which is specifically barred by the United States Bankruptcy Code. 11 U.S.C. § 362. (G) The Fourth Circuit's



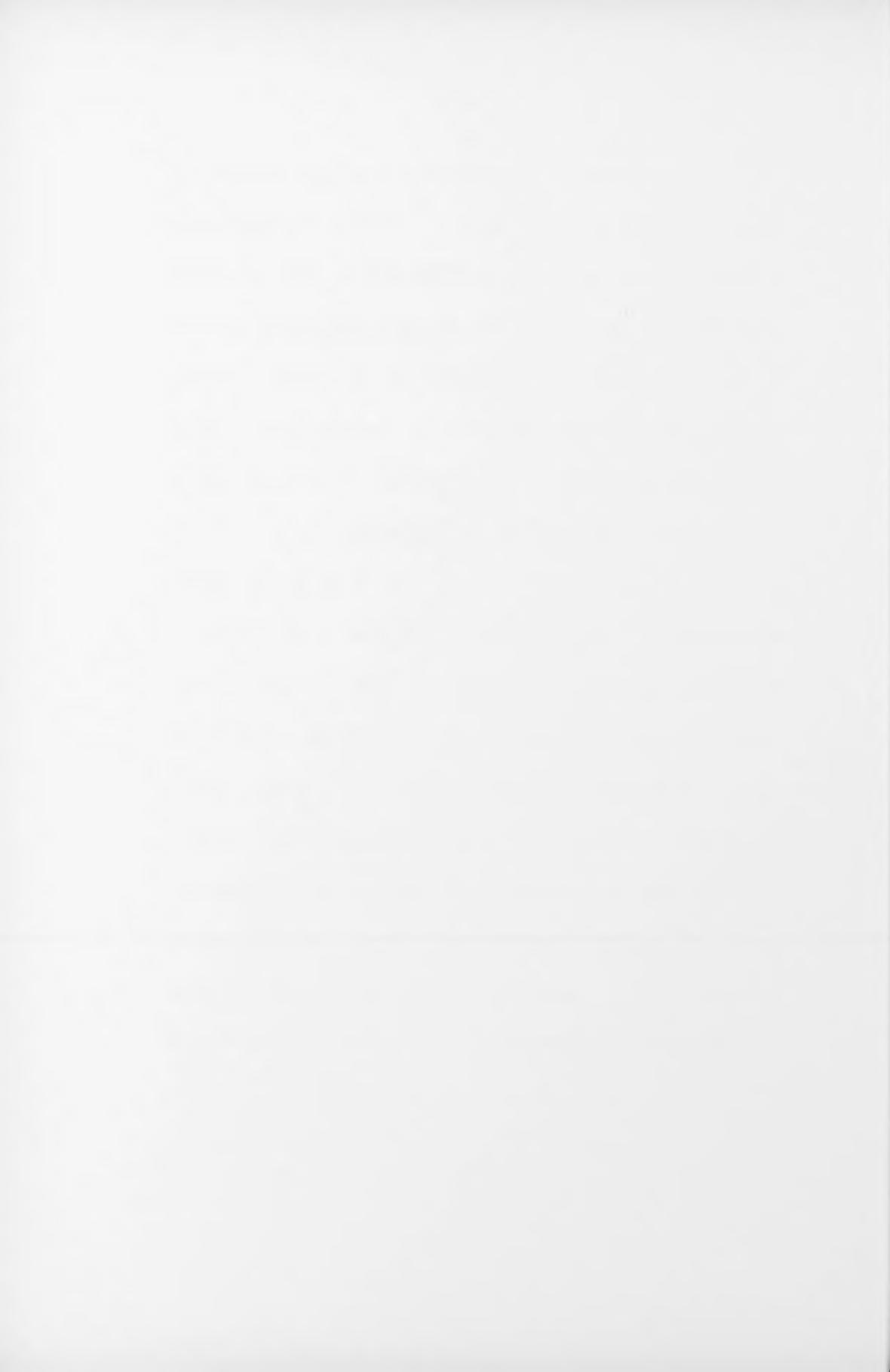
sanctioning of the United States District Court's Opinion which provided for the government seizure of estate property, ignoring all other Code provisions, wreaks havoc on the organization, priority and administration of estates under the Code. Without the guidance from the United States Supreme Court on this issue and the reversal of the Fourth Circuit Opinion, Trustees and Debtors-In-Possession must forfeit, upon demand, estate property to governmental units or entities.

This seizure can take place without any control by the Bankruptcy Court. It will result in judicially rewriting the priority scheme codified by the Bankruptcy Code. The Troxler decision, by allowing uncontrolled interference



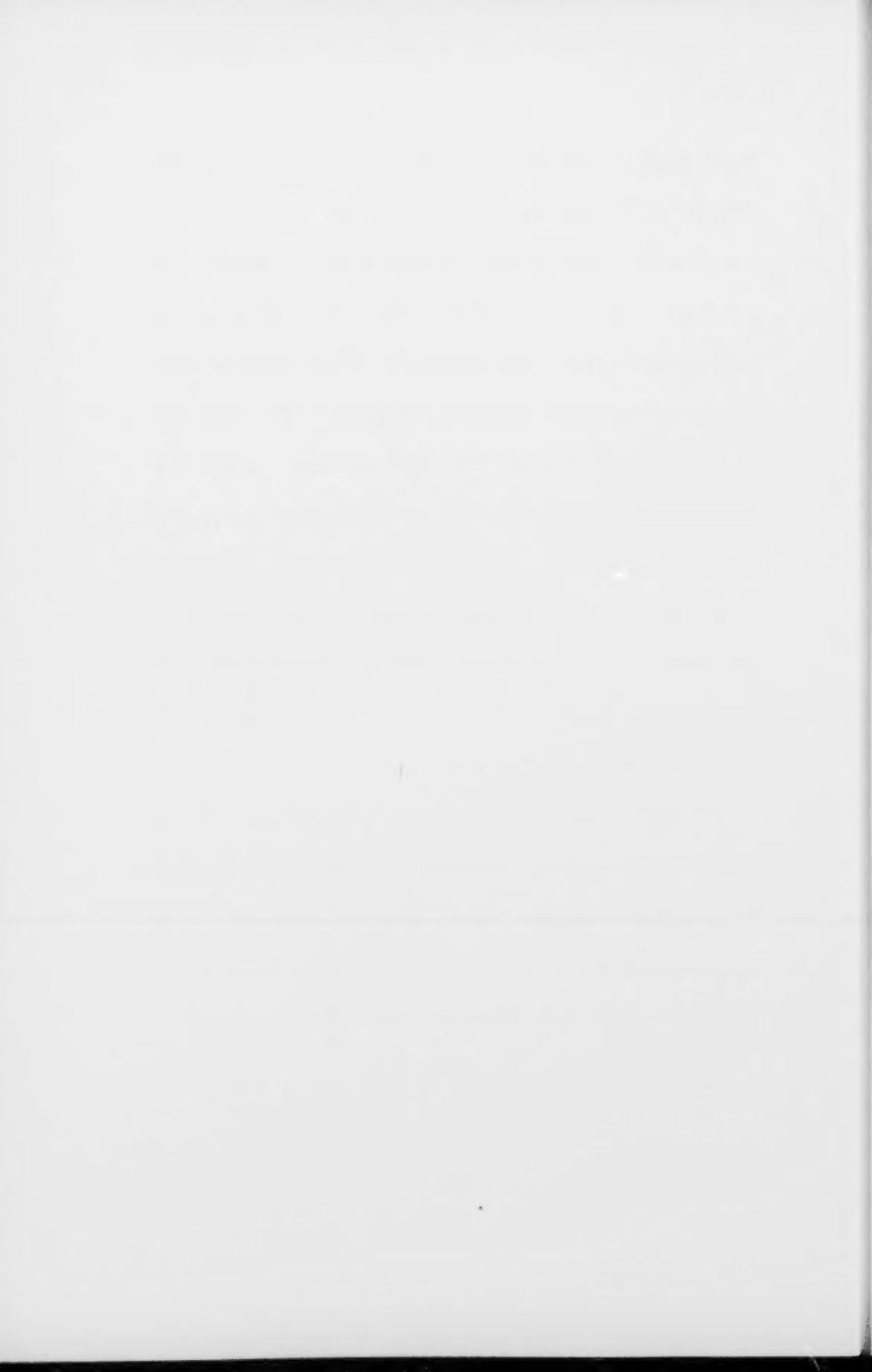
with estate property, makes it extremely difficult for a Trustee or Debtor-in-Possession to properly administer the estate for the benefit of creditors. Many bankruptcy cases will first have to be administered for the benefit of the governmental entity irrespective of all other creditors. The Troxler decision makes the Bankruptcy Court the safe haven for criminals to seek so that all creditors will be stayed from interfering with the property of the estate while the governmental entity can collect its fine. In effect, all competition for the debtor's property is eliminated. This result is contrary to 11 U.S.C. § 726(a)(4) which codifies the Congressionally intended order of distribution to creditors.

The Fourth Circuit, at the time of its decision and order denying rehearing, failed to consider the Second Circuit's opinion of In re Robinson, 776 F.2d 30 (2nd Cir. 1985) in affirming the lower Court's order. Recently, this honorable Court reversed the Robinson decision. Kelly v. Robinson, ____ U.S. ___, ____ S.Ct. ___, 54 U.S.L.W. 2257 (November 12, 1986) (No. 85-1033). Reviewing and reversing the decision of the Fourth Circuit in Troxler would be the needed resolution of the next logical dilemma in bankruptcy cases involving governmental entities. Due to the Troxler decision, the Bankruptcy Court will become the safe haven for criminals, contrary to the spirit of



Robinson, supra., which the 11 U.S.C. § 362(b)(1) exception to the automatic stay was designed to prevent. There is a dire necessity for the United States Supreme Court to rectify this situation to further the public policy of the 11 U.S.C. § 362(b)(1) exception and to preserve the orderly administration of bankruptcy proceedings. The United States Supreme Court should decide and settle this important question of federal law pursuant to Sup.Ct.R. 17.1(a) and (c).

For the foregoing reasons, this Honorable Court should grant certiorari to the Petitioner and reverse the decisions of the United States Court of Appeals for the Fourth Circuit.

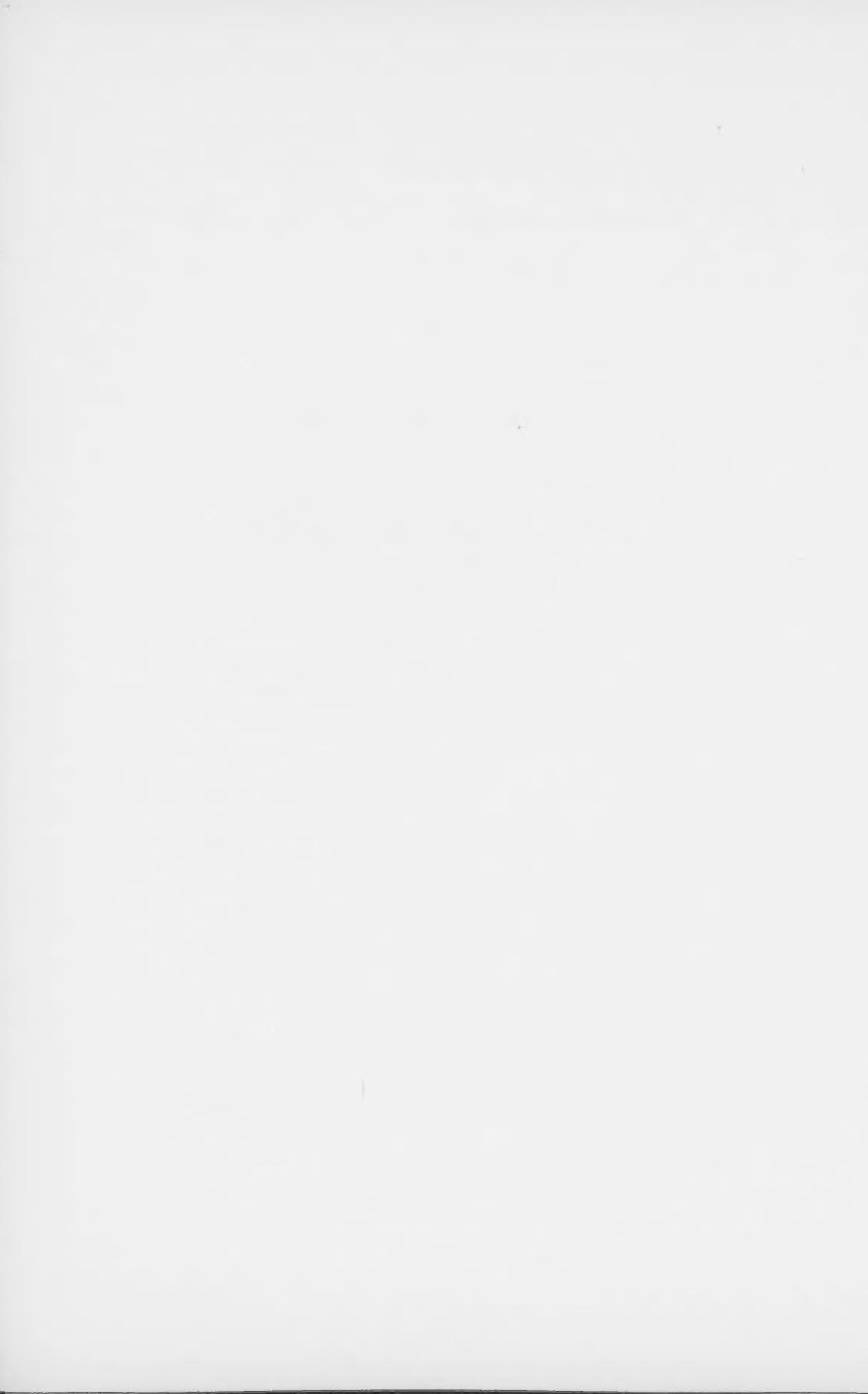


RESPECTFULLY SUBMITTED, this the 19th
day of December, 1986.

IVEY, IVEY & DONAHUE

BY:


CHARLES M. IVEY, III
Post Office Box 3324
Greensboro, N. C. 27402
(919) 274-4658



FILING AND MAILING CERTIFICATE

I, Barbara E. Grove, hereby certify that on this 19th day of December, 1986, I filed with the Clerk's Office of the Supreme Court of the United States the foregoing Petition for a Writ of Certiorari and further certify that I mailed this same date the required copies to the opposing counsel listed below:

Richard L. Robertson, Esquire
Assistant United States Attorney
Post Office Box 1858
Greensboro, North Carolina 27402

David P. Grise, Esquire
Office of Consumer Litigation
U. S. Department of Justice
Washington, D. C. 20530

John R. Fleder, Esquire
Office of Consumer Litigation
U. S. Department of Justice
Washington, D. C. 20530

Barbara E. Grove



A P P E N D I X



IN THE UNITED STATES BANKRUPTCY COURT
FOR THE MIDDLE DISTRICT OF NORTH CAROLINA

No. B-82-02002C-11
A-83-0510

In re:)
)
TROXLER HOSIERY CO., INC.)
P. O. Box 20012)
Greensboro, N. C. 27402)
)
Debtor.)
)
UNITED STATES OF AMERICA,)
)
Plaintiff,)
)
vs.)
)
TROXLER HOSIERY CO., INC.,)
)
Defendant.)

ORDER DENYING PLAINTIFF'S MOTION
FOR SUMMARY JUDGMENT

At Greensboro, N. C., this 5 day of
March, 1984.

The Court having heard arguments of
Counsel at the Hearing held in this
matter, after due notice, on December 5,
1983, and having continued the matter



Fourth Circuit imposed a fine of \$80,000.00, plus costs, on Troxler Hosiery Co., Inc. for willfully violating the Court's Order with respect to certain Tris-treated garments. By an Order dated August 5, 1982, the Circuit Court of Appeals for the Fourth Circuit ordered that Troxler Hosiery Co., Inc. (hereafter Troxler) pay the fine within twelve months. Troxler subsequently filed a motion to reduce the fine, and on November 15, 1982 the Circuit Court filed an Order denying Troxler's motion for reduction of the amount of the fine, but "without prejudice to its renewal upon presentation of additional or more persuasive proof."

3. On February 3, 1983, the United States Justice Department filed Proof of



Claim in these proceedings as a Secured Creditor in the amount of \$82,733.48 (fine and costs), based on liens claimed to have been obtained in September and October, 1982.

4. On October 5, 1983, the United States filed this Adversary Proceeding and Complaint therein seeking a declaratory judgment that the provisions of the Automatic Stay of Section 362 of the Bankruptcy Code did not apply to the claim of the United States for payment of \$82,733.48, for dismissal of the Chapter 11 proceedings, or in the alternative for an Order requiring a Plan of Reorganization to be filed within 30 days. Thereafter, Troxler filed Answer denying the material allegations of the Complaint.



5. On November 14, 1983, the United States filed and served its Motion For Summary Judgment as appears of record seeking adjudication as to its right to immediately collect the \$82,733.48 from assets of the Debtor's estate.

6. On December 3, 1983, Troxler and the Committee of Unsecured Creditors in these proceedings filed its Plan of Reorganization/Liquidation, and on January 6, 1984, filed Disclosure Statement in connection therewith.

7. Schedule A-2 of the Petition filed by the Debtor herein establishes that First Citizens Bank & Trust Company, Greensboro, N. C., Piedmont Paper Stock Company, Greensboro, N. C., and BarclaysAmerican/Commercial, Inc.,



Charlotte, N. C., have liens on the Guilford County real estate of Troxler which are superior to the claim of the Government asserted herein, the superior claims amounting to \$638,930.00. The Illinois property of the Debtor is encumbered by a first lien security interest of Illinois National Bank in the amount of \$37,807.00 and the security interest of R. A. Troxler, Sr. in the amount of \$94,986.55, both of which liens were recorded prior to the lien claimed by the Government. The lien asserted by R. A. Troxler, Sr. on the Springfield, Illinois, property has been attacked in the suit brought against R. A. Troxler, Sr. by the Committee of Unsecured Creditors, which is pending decision in this Court.



8. The claim of the Government herein in the amount of \$82,733.48 is a money judgment obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police power.

Upon the foregoing findings, the Court concludes as a matter of law that (1) there are no genuine issues as to material facts herein, (2) that the stay of Section 362 of the Bankruptcy Code applies to the Plaintiff herein on the facts as found herein, and it is not appropriate and in the interest of the Bankrupt's estate to lift the stay, and (3) that the Movant is not entitled to judgment as a matter of law;

IT IS, THEREFORE, ORDERED that the Motion for Partial Summary Judgment of



the Plaintiff herein be, and the same is, hereby denied.

Nothing in this Order shall be construed to prohibit the United States from taking any action herein other than action directed against the property of the estate of the Debtor-in-Possession.

/s/ Rufus W. Reynolds
United States Bankruptcy Judge

UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF NORTH CAROLINA
GREENSBORO DIVISION
No. C-84-322-G
B-82-02002C-11

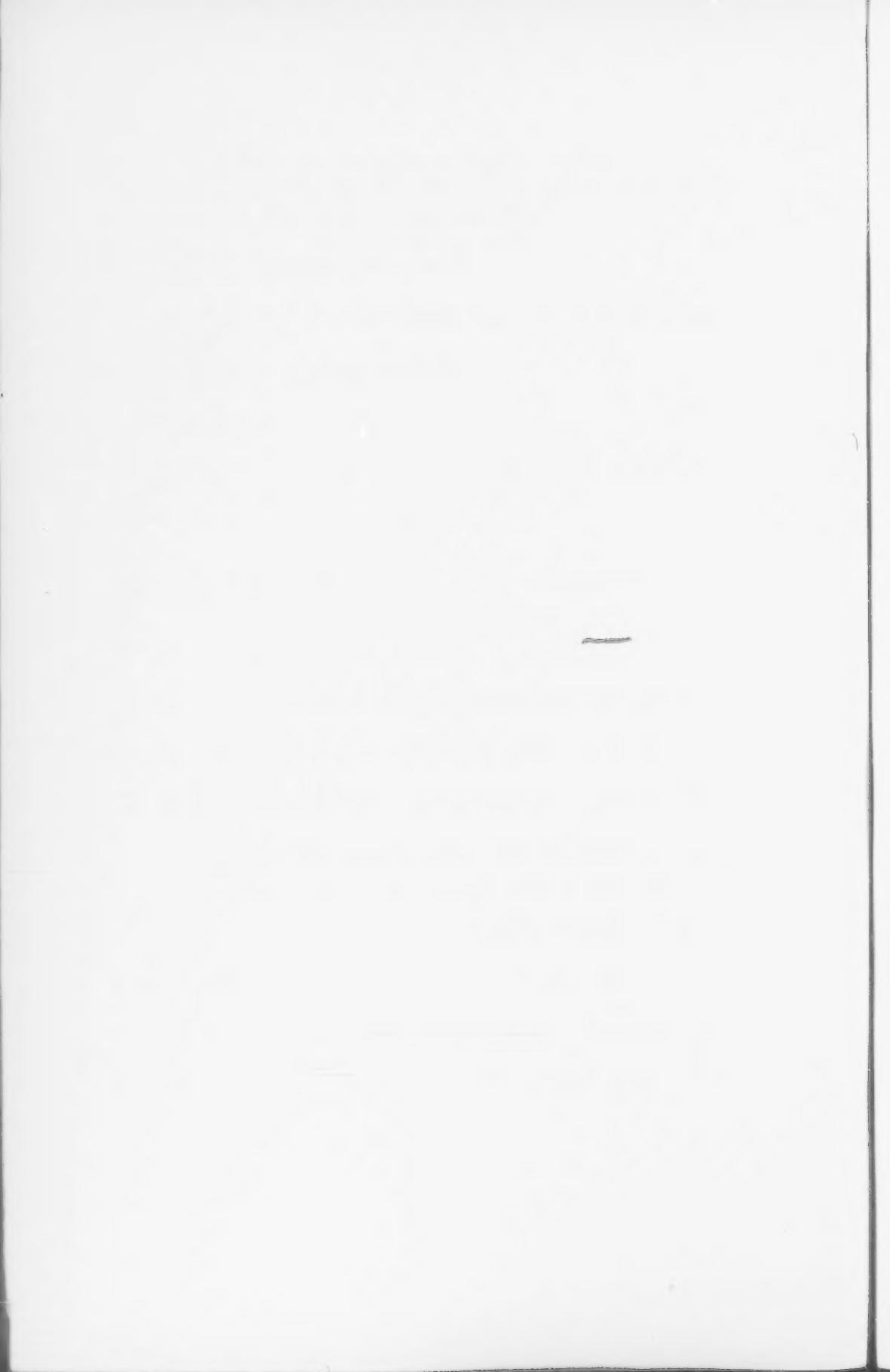
UNITED STATES OF AMERICA, :
:
Appellant, :
:
v. :
:
TROXLER HOSIERY CO., INC., :
:
Appellee :
:

Filed July 27, 1984

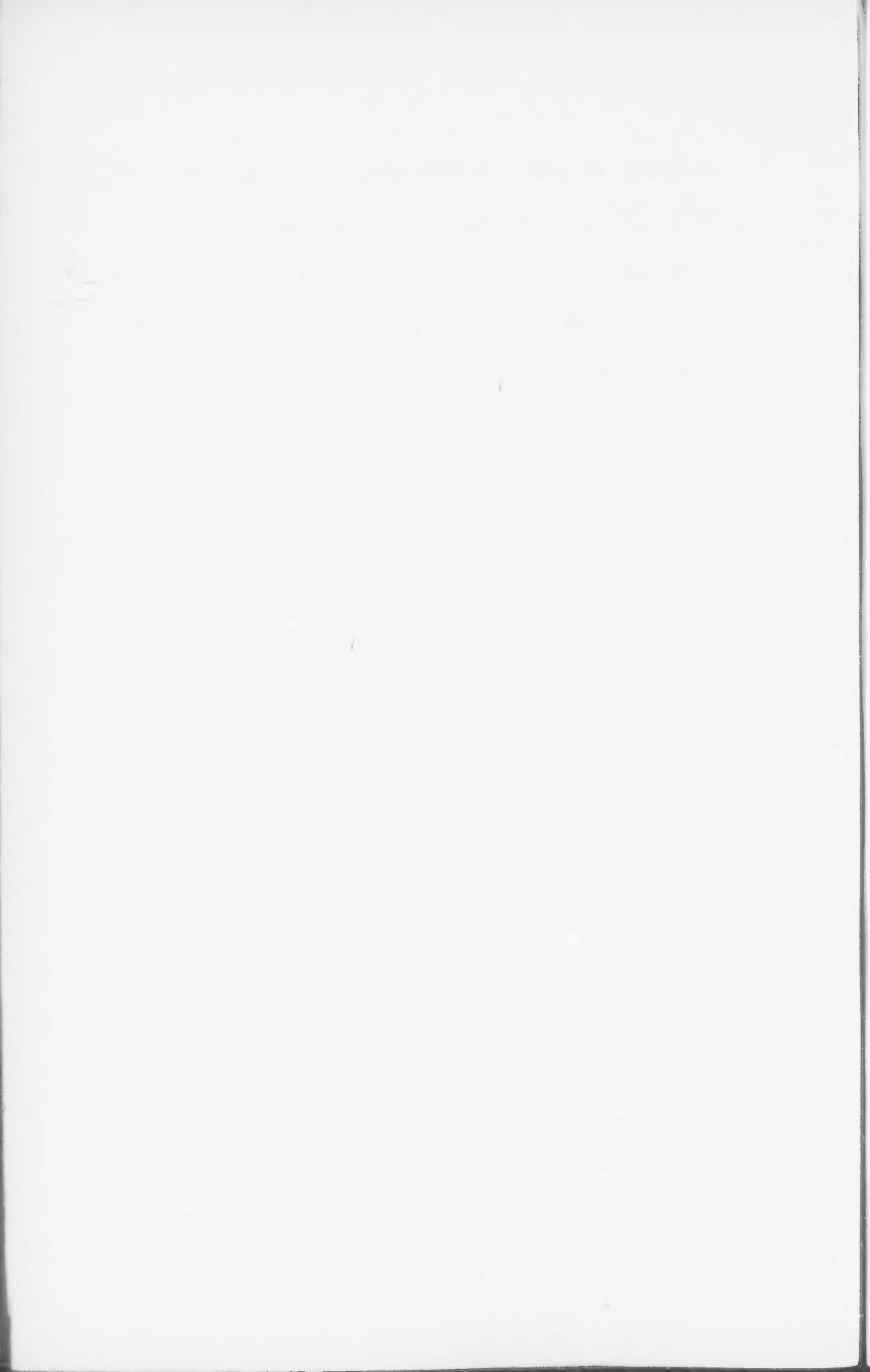
Appeal from the United States Bankruptcy
Court for the Middle District of North
Carolina, Greensboro Division, Hiram H.
Ward, United States District Judge

WARD, Chief Judge

This matter came before the Court
on appeal from the March 5, 1984 Order
of the Honorable Rufus W. Reynolds,



United States Bankruptcy Judge, denying plaintiff's Motion for Summary Judgment (Record on Appeal, Item 11). The Bankruptcy Court's order denied the United State's request for a declaratory judgment relieving it from the automatic stay of 11 U.S.C. § 362(a). The government seeks to collect a criminal fine and costs imposed on Troxler Hosiery Co., Inc. (Troxler), the debtor appellee, and contends that 11 U.S.C. § 362(b)(1) excepts such collection from the automatic stay. Gerald S. Schafer, Trustee for Troxler, asserts that collection of the criminal fine is not a criminal proceeding excepted by 11 U.S.C. § 362(b)(1). The Trustee further asserts that the fine is a money judgment of a governmental unit which



under 11 U.S.C. § 362(b)(1) is not excluded from the automatic stay. The Court, having reviewed the Record on Appeal, considered the parties' briefs and heard arguments of counsel on June 26, 1984, will reverse the Bankruptcy Court's order.

In January, 1978, the government commenced forfeiture proceedings against TRIS-treated sleepwear garments possessed by Troxler which it contended were hazardous substances. A district court order quashing the warrant of seizure was appealed to the United States Court of Appeals for the Fourth Circuit. On February 2, 1978, the Honorable Harrison A. Winter, United States Circuit Judge, entered an order prohibiting Troxler from removing the



seized garments from the Middle District of North Carolina. This order was continued on March 8, 1978. On remand to the district court for the limited purpose of determining the appropriate disposition of the goods in the event they were subsequently found to be subject to condemnation, the district court concluded that the goods could not be released to Troxler for sale in foreign commerce. The Court Appeals agreed with this particular ruling of the district court. United States v. Articles of Hazardous Substance, etc. and Troxler Hosiery Co., 588 F.2d 39, 44 (4th Cir. 1978). In May, 1978, while Judge Winter's order was still in effect, Troxler, through the direction of its president, Robert A. Troxler,



Sr., arranged for the sale and removal of the seized garments to Miami and Venezuela. The Fourth Circuit later ruled that the seizure of the goods was lawful. United States v. Articles of Hazardous Substance, 588 F.2d 39.

Criminal contempt proceedings against Troxler were instituted in the Fourth Circuit in May 1981. Troxler was found guilty of criminal contempt under 18 U.S.C. § 401(3)¹. United States v. Troxler Hosiery Co., 672 F.2d 365 (4th Cir. 1982), and fined \$80,000.00 plus costs. United States v. Troxler Hosiery

¹ "A court of the United States shall have power to punish by fine or imprisonment, at its discretion, such contempt of its authority, and none other, as ... (3) Disobedience or resistance to its lawful writ, process, order, rule, decree or command." 18 U.S.C. §401(3).



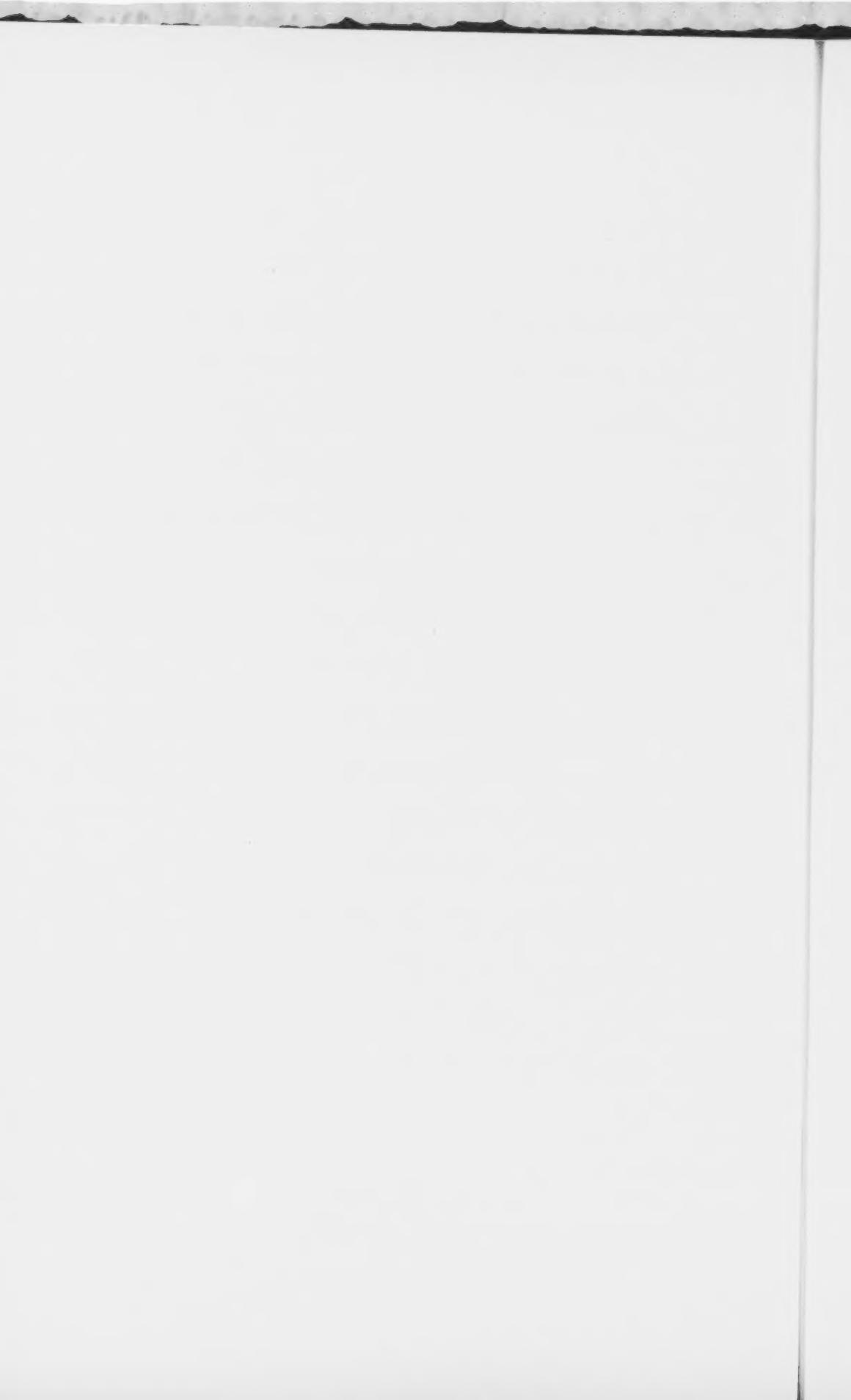
Co., 681 F.2d 934 (4th Cir. 1982). In setting the fine, the court considered Troxler's ability to pay. 681 F.2d at 938. Troxler was given twelve (12) months from the date of the Judgment, August 5, 1982, to pay the fine and costs totalling \$82,733.48. Troxler's motion to reduce the fine, Fed.R.Crim.P. 35, was denied on November 15, 1982.

Troxler filed a voluntary petition under Chapter 11 of the Bankruptcy Code on November 3, 1982. On February 3, 1983, the government filed a proof of secured claim in the amount of the fine and costs, none of which had been paid. On October 5, 1983, the government filed an adversary proceeding complaint in bankruptcy seeking a declaratory judgment that the automatic stay did not



apply to its attempts to collect the criminal fine. The bankruptcy proceeding was converted to a Chapter 7 liquidation proceeding on March 12, 1984.

Following two rounds of briefing and oral arguments, the Bankruptcy Court denied the government's request and ruled as a matter of law that the automatic stay applied to the United States' efforts to collect the contempt fine. The Bankruptcy Court order stated that the government's claim is a money judgment obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police power under section 11 U.S.C. § 362(b)(5) which provides:

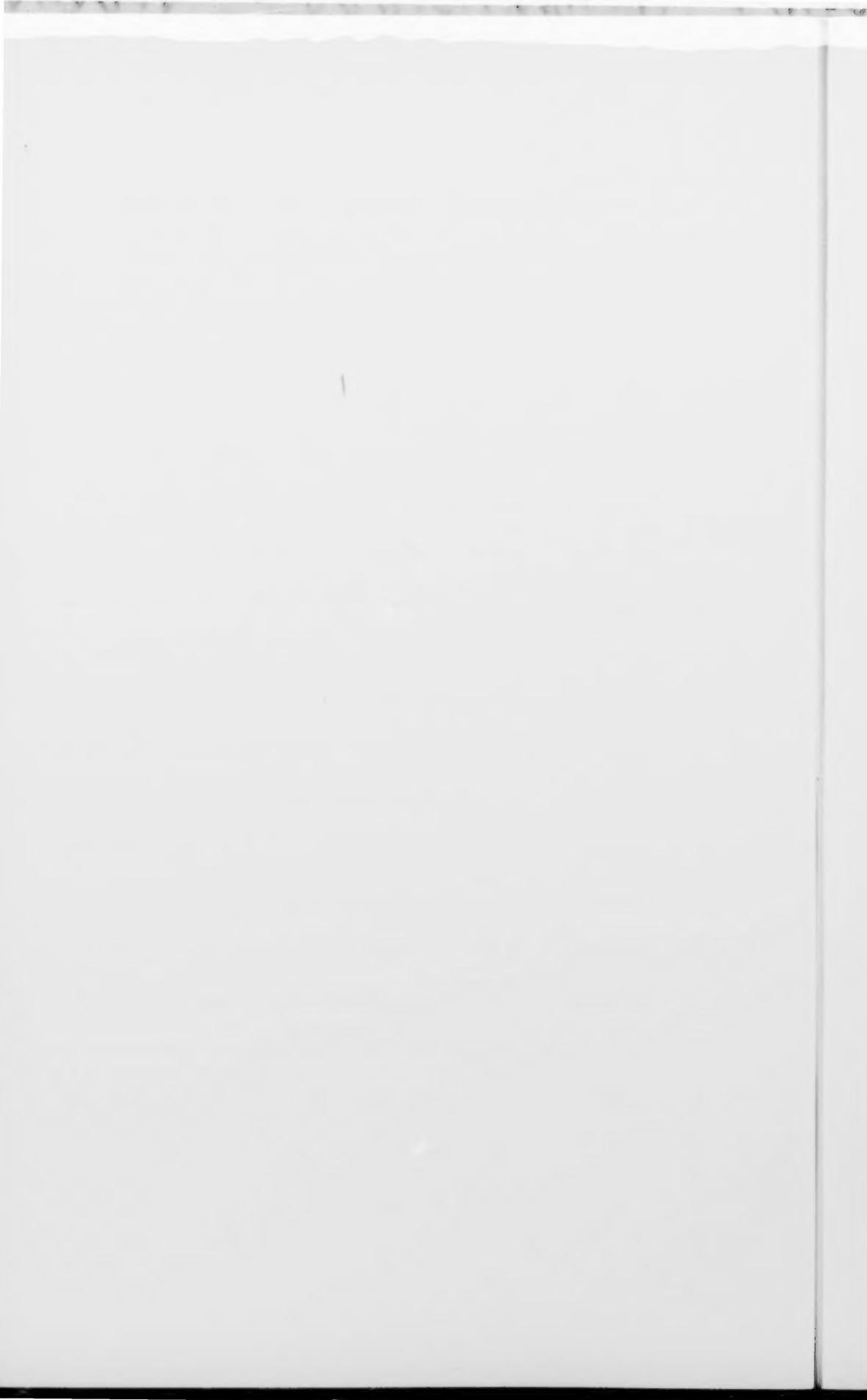


Under subsection (a)(2) of this section, ... the enforcement of a judgment, other than a money judgment, obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power is not stayed.

The Bankruptcy Court inappropriately relied on this subsection. A criminal contempt case is different from an action of a governmental unit to enforce its police or regulatory powers. The phrase "police or regulatory power" refers to the administration and enforcement of "state laws affecting health, welfare, morals, and safety" Missouri v. U.S. Bankruptcy Court, 647 F.2d 768, 776 (8th Cir. 1981), cert. denied, 454 U.S. 1162 (1982). The pertinent legislative history of the statute describes "police

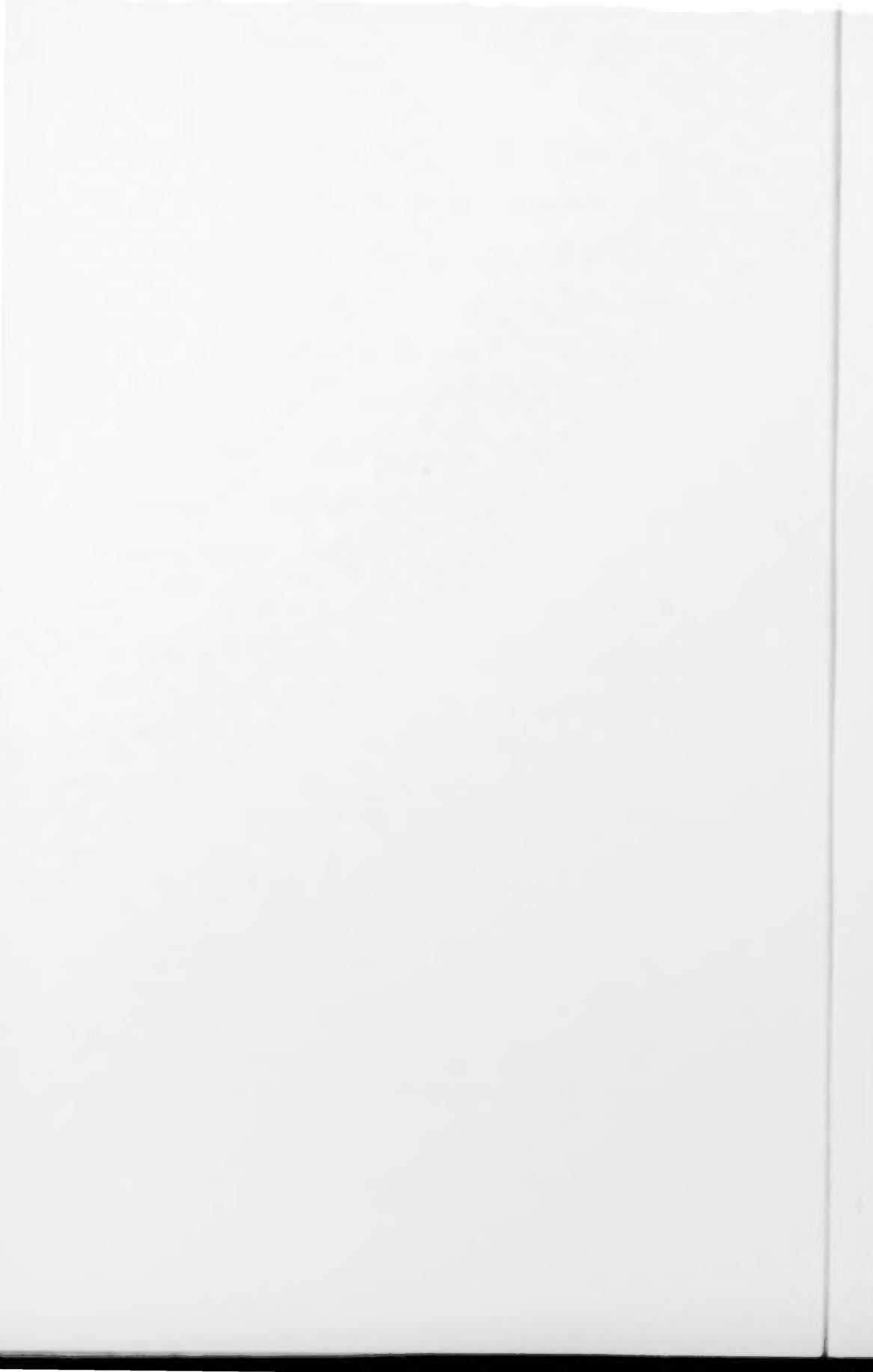


or regulatory power" as governmental action relating to consumer protection, environmental protection, fraud, safety, or similar police or regulatory laws. H.R. Rep. No. 95-595, 95th Cong., 2d Sess. 343, reprinted in 1978 U.S. Code Cong. & Ad. News 5787, 6299; S. Rep. No. 95-989, 95th Cong., 2d Sess. 52, reprinted in U.S. Code Cong. & Ad. News 5787, 5838. Section 362(b)(5) permits a direct application of a governmental unit's police or regulatory powers against a debtor but prohibits actions aimed at obtaining a pecuniary advantage. In re Aegean Fare, Inc., 35 Bankr. 923 (Bankr. D.Mass. 1983). Prosecution of a criminal case is not, however, aimed at obtaining a pecuniary advantage. It is designed to punish



offenders of the criminal law and serve as a deterrence to others. If Congress intended for police power to include enforcement of criminal laws, 11 U.S.C. § 362(b)(1) would be surplusage. While sections 362(b)(1) and (5), 11 U.S.C., are indeed related since they identify situations when proceedings against an estate are not stayed, they concern different topics. Only section 362(b)(1) is relevant to the issue in this case.²

² Although the only citation of authority in the Bankruptcy Court Order of March 5, 1984 is 11 U.S.C. § 362(b)(5), it appears that its decision was at best only collaterally based on that statute. During the second round of oral arguments Judge Reynolds heard in this matter, he stated that the Section 362(b)(1) criminal exception applied to procedure but not to collection. In his view, criminal proceedings can commence or continue so long as the property of the estate is



The Court's task in a case of statutory construction is to interpret the words of the statute in light of the purposes Congress sought to serve.

Norfolk Redevelopment and Housing Authority v. Chesapeake and Potomac Telephone Co., _____ U.S. _____, 104 S.Ct. _____, 78 L.Ed.2d 29, 34 (1983).

The starting point for interpreting a statute is the language of the statute itself. Consumer Product Safety

not bothered. From the bench, Judge Reynolds stated that section 362(b)(1) allows the government to continue with their proceedings but that they are limited to procedure. Transcript of Hearing on Judgment on Request for Declaratory Judgment at 4 (Record on Appeal, Item (9)).

The order prepared for the Bankruptcy Court does not reflect this line of reasoning but cites 11 U.S.C. § 362(b)(5) which was brought to Judge Reynolds' attention after he had voiced his reasoned decision



Commission v. GTE Sylvania, Inc., 447 U.S. 102, 108, 100 S.Ct. 2051, ___, 64 L.Ed.2d 766, 772 (1980).

Section 362(b)(1), 11 U.S.C., provides that "the filing of a petition in bankruptcy ... does not operate as a stay ... under subsection (a) of this section, of the commencement or continuation of a criminal action or proceeding against the debtor." It is undisputed that the contempt proceedings against Troxler were criminal in nature. Sentencing of a criminal defendant, whether it be imprisonment or imposition of a fine, fixes and declares the legal consequences of predetermined guilt.

United States v. Henry, 709 F.2d 298, 310 (5th Cir. 1983). A criminal sentence without accompanying authority



to ensure service by the defendant as ordered would be meaningless. Action by the government to enforce the terms of a sentence are plainly a continuation of the entire criminal proceeding. The fact that the government may resort to collection means which are civil in nature³ does not transform a criminal case into a civil one.

The Trustee's position is that 11 U.S.C. § 362(b)(1) excepts from the automatic stay a criminal prosecution against the debtor and service of a prison term but does not lift the stay for the purposes of collecting money from a criminal/debtor (or

³ The payment of a criminal fine "may be enforced by execution against the property of the defendant in like manner as judgments in civil cases". 18 U.S.C. § 3565.

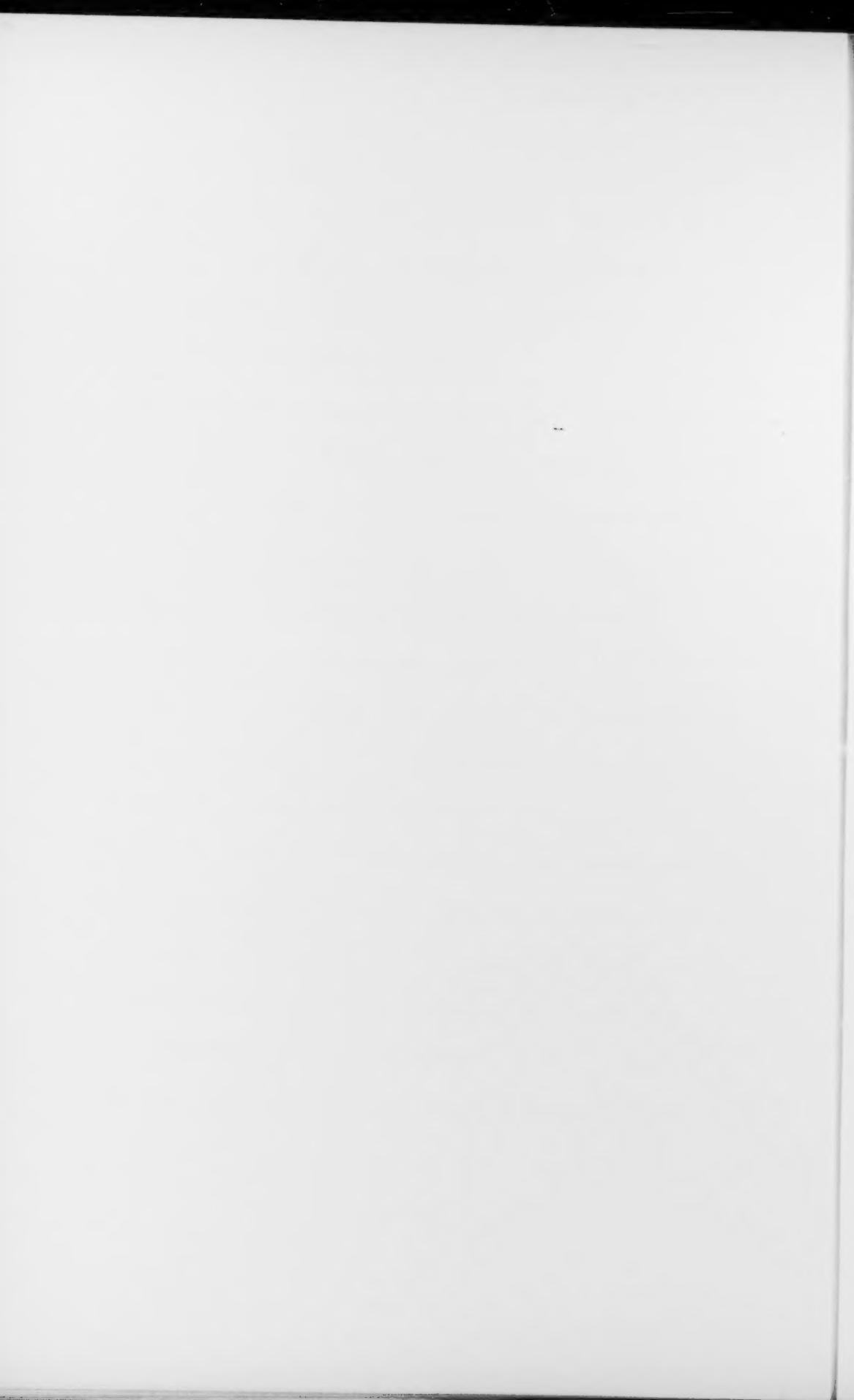


property of its estate) because of the detrimental effect such as collection would have on the bankruptcy administration. The language of the statute does not support the Trustee's position. It makes no distinction between sentences or imprisonment or fines and is broad enough to include enforcement of a judgment through pecuniary collection means from the debtor or property of the estate. Section 362(a), 11 U.S.C., contains eight subsections, all of which define different proceedings. Noteworthy here are subsections (1) and (2). Subsection (1) stays judicial, administrative, and other proceedings to recover a claim against the debtor. Subsection (2) stays "the enforcement, against the



debtor or property of the estate, of a judgment obtained before the commencement of the bankruptcy case..." Thus, section 362(a)(2) standing alone stays enforcement procedures of the nature which the government would like to employ against Troxler.

The eight subsections of 11 U.S.C. 362(b) identify matters which are not affected by part or all of the stays variously enunciated in 11 U.S.C. § 362(a). The section 362b(b)(1) criminal proceedings exception applies without limitation to any specific subsection of section 362(a). The breadth of section 362(b)(1) is significant when contrasted with the exceptions set forth in sections 362(b)(4) & (5) which do not



refer to the all inclusive nature of section 362(a) but which are specifically limited in their application to subsections 362(a)(1) & (2), respectively.

When Congress includes particular language in one section but omits it in another section of the same act, it is generally presumed that Congress acted intentionally and purposefully in the inclusion and exclusion. Russello v. United States, ____ U.S. ___, 104 S.Ct. ___, 78 L.Ed.2d 17, 14 (1983). "The drafting of the exceptions to the various stays of section 362(a) is precise and intentional and must be carefully considered in light of the inclusive nature of section 362(a)." 2 Collier on Bankruptcy § 362.05 at 362-38



(1984) (emphasis added). Unlike the restrictions found in sections 362(b)(4) & (5), Congress did not, in section 362(b)(1), limit the scope of the criminal proceedings exception to the automatic stay. Precise application of section 362(b)(1) excepts criminal proceedings from all of the various automatic stays, including the otherwise operative stay of judgment enforcement proceedings against the debtor or property of the estate of 11 U.S.C. § 362(a)(2). See 2 Bankruptcy - L.Ed. Summary § 6:135 at 151 (1981) (if action or proceeding is criminal, it is insulated from all of the automatic stays provisions).

This interpretation of 11 U.S.C. § 362(b)(1) is consistent with the

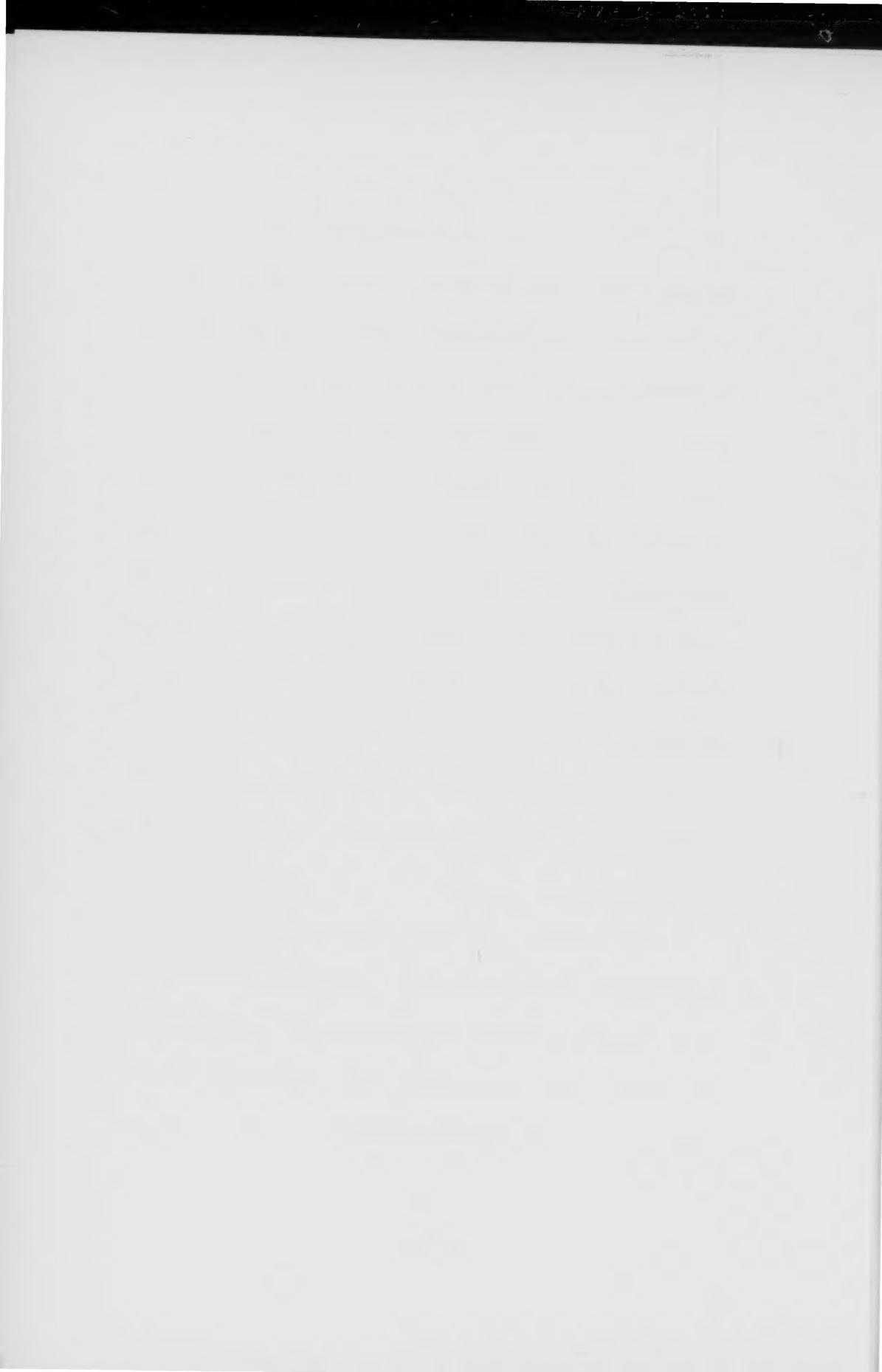


legislative history and the practice under the former Bankruptcy Act. "The bankruptcy laws are not a haven for criminal offenders but are designed to give relief from financial over extension. Thus, criminal actions and proceedings may proceed in spite of bankruptcy." H.R. Rep. No. 95-595, 95th Cong. 2d Sess. 343, reprinted in 1978 U.S. Code Cong. & Ad. News, 5787, 6299; S. Rep. No. 95-989, 95th Cong. 2d Sess. 51, reprinted in 1978 U.S. Cong. & Ad. News, 5787, 5837. Although it is true that a stay under the Bankruptcy Act depended on notions of provability, allowability, and dischargeability (concepts which do not concern the operation of 11 U.S.C. § 362(a)) the underlying principle of 11 U.S.C. §



362(b)(1), that bankruptcy is not a haven for criminals, was also viable under the Bankruptcy Act. See In re Thomashefsky, 51 F.2d 1040 (2d. Cir. 1931), (a contempt fine is not a dischargeable debt, consequently its collection is not stayed); In re Koronsky, 170 F. 719 (2d Cir. 1909) (enforcement of contempt fine ordered by state court not stayed by bankruptcy); In re Licht, 19 F.Supp. 774 (E.D.N.Y. 1937) (bankruptcy does not relieve bankrupt of punishment for contempt and perjury).

In spite of the criminal nature of contempt proceedings against Troxler, the Trustee contends that the government is merely a creditor of Troxler in a typical debtor/creditor relationship.



This contention ignores the realities of the criminal law. A criminal sentence, whether it be imprisonment or fine, is not direct compensation for a pecuniary loss but is punishment for violation of the criminal law. A criminal sentence serves interests which are not based on compensation for a debt which is normally dischargeable in bankruptcy. While there is a surprising absence of contemporary controlling or persuasive case authority on the scope of 11 U.S.C.



§ 362(b)(1),⁴ according due deference to the purposes of the criminal law has led some courts to find that a criminal sentence is not a debt contemplated by the Bankruptcy Code, and, therefore, is not subject to the stay or discharge provisions of bankruptcy. In re Magnifico, 21 Bankr. 800, 803 (Bankr. D.Ariz. 1982); In re Button, 8 Bankr. 692 (Bankr. W.D.N.Y. 1981) (restitution is not a debt and victim is not a

⁴ The Trustee cites E.E.O.C. v. Rath Packing Co., 37 Bankr. 614, 616 (Bankr. S.D.Iowa 1984), and S.E.C. v. First Financial Group, 645 F.2d 429, 437 (5th Cir. 1981), for the dicta contained in each there is no exemption from the automatic stay for proceedings to enforce a judgment against property of the estate. Criminal proceedings were not in issue in either of these cases. The Court rejects the applicability of these cases because without explanation they ignore the contrasting applicabilities of the 11 U.S.C. 362(b) exceptions to the various stays of 11 U.S.C. § 362(a).

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creditor). Similarly, because a criminal prosecution is designed to promote the public welfare by punishing offenders and deterring others, it has been held that bankruptcy should not interfere with prosecution of a bad check case, even if restitution could be ordered, because an "absurd paradox would result, i.e., one who has engaged in criminal conduct could escape punishment by the mere filing of a bankruptcy petition." In re Richardello, 28 Bankr. 344 (Bankr. D.Mass. 1983) (criminal laws intended to protect commercial transactions and fact that possible sentence was restitution to one who coincidentally was creditor in bankruptcy did not justify stay of criminal action); In re Newton, 15



Bankr. 708 (Bankr. N.D.Ga. 1981) (order of restitution if part of criminal sentence and is not stayed); cf. In re James, 10 Bankr. 2 (Bankr. W.D.N.C. 1980) (where criminal action is merely guise to collect civil debt, criminal action and collection attempts stayed).

The Court concludes that enforcement of the sentence declared in the pre-petition criminal contempt judgment against Troxler or the property of its estate in bankruptcy is excepted from the automatic stay by 11 U.S.C. § 362(b)(1). The importance and legitimacy of the interests forwarded by both parties make this conclusion a most difficult one to reach. However, enforcement of a sentence is plainly a continuation of a criminal proceeding



and the language and structure of 11 U.S.C. § 362(b)(1) provides for such enforcement in spite of bankruptcy. The Court has considered the potentially detrimental effect which relieving the government from the automatic stay could have on the unsecured creditors. Creditors of equal standing should not be treated unequally and creditors should not be indirectly punished for the criminal wrongs of the bankrupt. Nevertheless, when the government is due payment of a criminal fine, it is not on an equal footing with most of a bankrupt's creditors because a criminal fine is not compensation for pecuniary loss. A sovereign's interest in protecting its citizens through the criminal law is fundamentally different



from private financial concerns and for that reason must take precedence. Moreover, it is not altogether accurate to argue that payment of a criminal fine punishes the creditors for the debtor's wrongdoing. In the instant case, Troxler's contemptuous conduct possibly increased its assets, now property of the estate subject to distribution to creditors.⁵

The Court recognizes that fines, penalties, forfeitures, and exemplary damages which are not compensation for actual pecuniary losses are distributed

⁵ The ultimate disposition of the garments Troxler shipped to Venezuela in flagrant disregard of a court order is unclear. They have been valued at \$144,716. Troxler officials stated that no profit had been realized, although some of the garments may have been sold. United States v. Troxler Hosiery Co., Inc., 681 F.2d 934, 937 (4th Cir. 1982).



after general unsecured claims under 11 U.S.C. § 726(a)(4) and, in the case of an individual debtor, are nondischargeable debts under 11 U.S.C. § 523(a)(7). The fact that such claims are distributed after general unsecured creditors may suggest, not unreasonably, that these claims are subordinated because they are nondischargeable.⁶

⁶ All claims against Troxler, including the government's claim, are nondischargeable because the bankrupt is a corporation as opposed to an individual, not because the fine does not represent a pecuniary loss to the government. 11 U.S.C. § 727(a)(1). Typically, any additional attempts of collection from a corporation are irrelevant because it is defunct.

The contempt proceedings were instituted against the corporate entity. The Court has no way of knowing whether they could have also been instituted against one or more of Troxler's officers but notes that if such was possible, this entire controversy may have been avoided.



However, the Court cannot rule that nondischargeability of a criminal fine is a basis for postponing the enforcement of a criminal judgment. The secondary yet surviving characteristics of a fine under 11 U.S.C. §§ 523(a)(7) and 726(a)(4) are not expressly directed at criminal fines but apply to any claim which is not based on pecuniary loss. The legislative history of these statutes supports no inference that these sections compliment 11 U.S.C. § 362(a). Moreover, the fact that the government's enforcement of criminal judgments is excepted from the stay is not inconsistent with the nondischargeability of a criminal fine because the government, in spite of the stay exception, may, for one reason or



another, not have collected its judgment in full prior to litigation. If that is the situation, the fine survives bankruptcy not because it coincidentally is criminal but because it, like the other claims identified in 11 U.S.C. §§ 523(a)(7) & 726(a)(4), is not direct compensation for pecuniary loss. Congress recognized that the interests served by the criminal law are paramount to those furthered in bankruptcy and 11 U.S.C. § 362(b)(1) is designed to accommodate these paramount interests. Manifestly, the statute prevents not only a complete bar of criminal proceedings, but also operates to preclude a substantial hinderance or delay in the enforcement of a criminal



judgment.⁷

⁷ The combined operation of 11 U.S.C. §§ 523(a)(7) and 726(a)(4) presents a potentially troubling and ironic situation. Since a criminal fine is in fact not direct compensation for actual pecuniary loss, one possible net effect of excepting the government from the automatic stay would be the discharge of all or part of some claims which otherwise might have been paid. Conceivably, an individual cognizant of the nondischargeability of a criminal fine might attempt to use bankruptcy to simultaneously dispose of a criminal fine and other debts (which are dischargeable) at the lowest possible cost. Theoretically, exception of the enforcement of a criminal judgment would facilitate such a scheme. The Court does not pass on the legal effect, if any, of such intent on the part of the debtor because there is no finding or indication that Troxler was so motivated. In fact, the government suggested that Troxler was motivated by an intent to evade criminal punishment rather than to facilitate payment of its judgment. The Court can only pass on the facts of the instant case and under these facts, 11 U.S.C.S 362(b)(1) excepts enforcement of a pre-bankruptcy petition criminal judgment from the automatic stay.

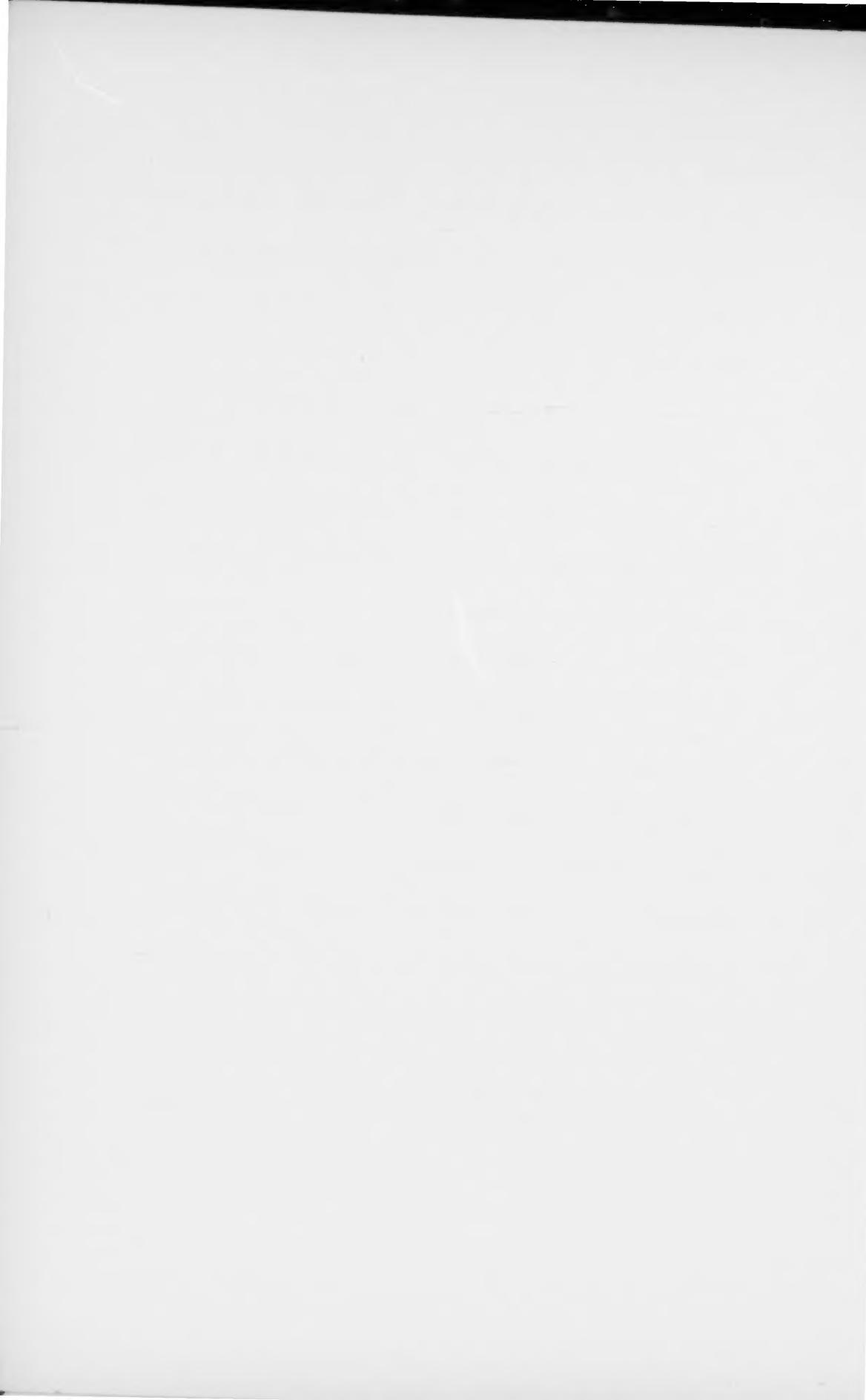


IT IS, THEREFORE, ORDERED that the Bankruptcy Court's Order of March 5, 1984, be, and the same hereby is, REVERSED.

IT IS DECLARED AND ADJUDGED that the automatic stay of 11 U.S.C. § 362 does not apply to collection of the appellant's \$82,733.48 criminal judgment claim from the appellee.

IT IS FURTHER ORDERED that the effect of this Order is stayed for ten (10) days from the date of its entry to allow the appellee, if it desires, an opportunity to seek a stay pending appeal to the United States Court of Appeals for the Fourth Circuit pursuant to Rule 8, Fed.R.App.Proc.

/s/ Hiram H. Ward
United States District Judge



UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 84-1846

United States of America,

Appellee,

Versus

Troxler Hosiery Co., Inc.,
and Gerald S. Schafer, trustee,

Appellants.

Appeal from the United States District Court for the Middle District of North Carolina, at Greensboro. Hiram H. Ward, District Judge. (C/A 84-322).

Argued: June 5, 1986

Decided: August 4, 1986

Before WINTER, Chief Judge, and WIDENER and CHAPMAN, Circuit Judges.

Charles M. Ivey, (Ivey, Ivey & Johns on brief) for Appellants; John R. Fleder, Office of Consumer Litigation, Civil Division, United States Department of Justice (Richard K. Willard, Acting Assistant Attorney General; Kenneth W.



McAllister, United States Attorney; Richard L. Robertson, Assistant United States Attorney; David P. Grise, Office of Consumer Litigation on brief) for Appellee.

PER CURIAM:

Troxler Hosiery Company, Inc., was convicted of criminal contempt¹ and fined \$80,000.00 plus costs² for removing previously seized hazardous sleepwear and contracting for its sale in a foreign country and for falsifying company records to conceal its actions. Troxler was given twelve months to pay the fine, but on November 3, 1982, it filed a voluntary petition under Chapter 11 of the Bankruptcy Code. The

¹ United States v. Troxler Hosiery Co., 672, F.2d 365 (4th Cir. 1982).

² United States v. Troxler Hosiery Co., 681 F.2d 934 (4th Cir. 1982).



government filed a proof of a secured claim in the amount of the fine and costs, no part of which has been paid. Later, the government filed an adversary proceeding complaint in bankruptcy seeking a declaratory judgment that the automatic stay did not apply to its attempts to collect the criminal fine. In March, 1984, the bankruptcy proceeding was converted to a Chapter 7 liquidation.

The bankruptcy court ruled as a matter of law that the automatic stay applied to the government's efforts to collect a contempt fine. On appeal to the United States District Court for the Middle District of North Carolina, the order of the bankruptcy court was reversed. The district judge found that



the automatic stay of 11 U.S.C. § 362 (1982 & Supp. II 1984) did not apply to the collection of the fine and costs for criminal contempt and that such fine survived the bankruptcy.

Troxler appealed, and the government filed a motion to supplement the record on appeal to include portions of depositions of Robert Andrew Troxler, Sr., and Robert Andrew Troxler, Jr. We conclude that the information contained in the supplement is not necessary to a decision in this case, and we deny the motion.

We adopt the excellent opinion of Chief Judge Hiram H. Ward filed July 28, 1984, and we affirm.

AFFIRMED



UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 84-1846

United States of America,

Appellee,

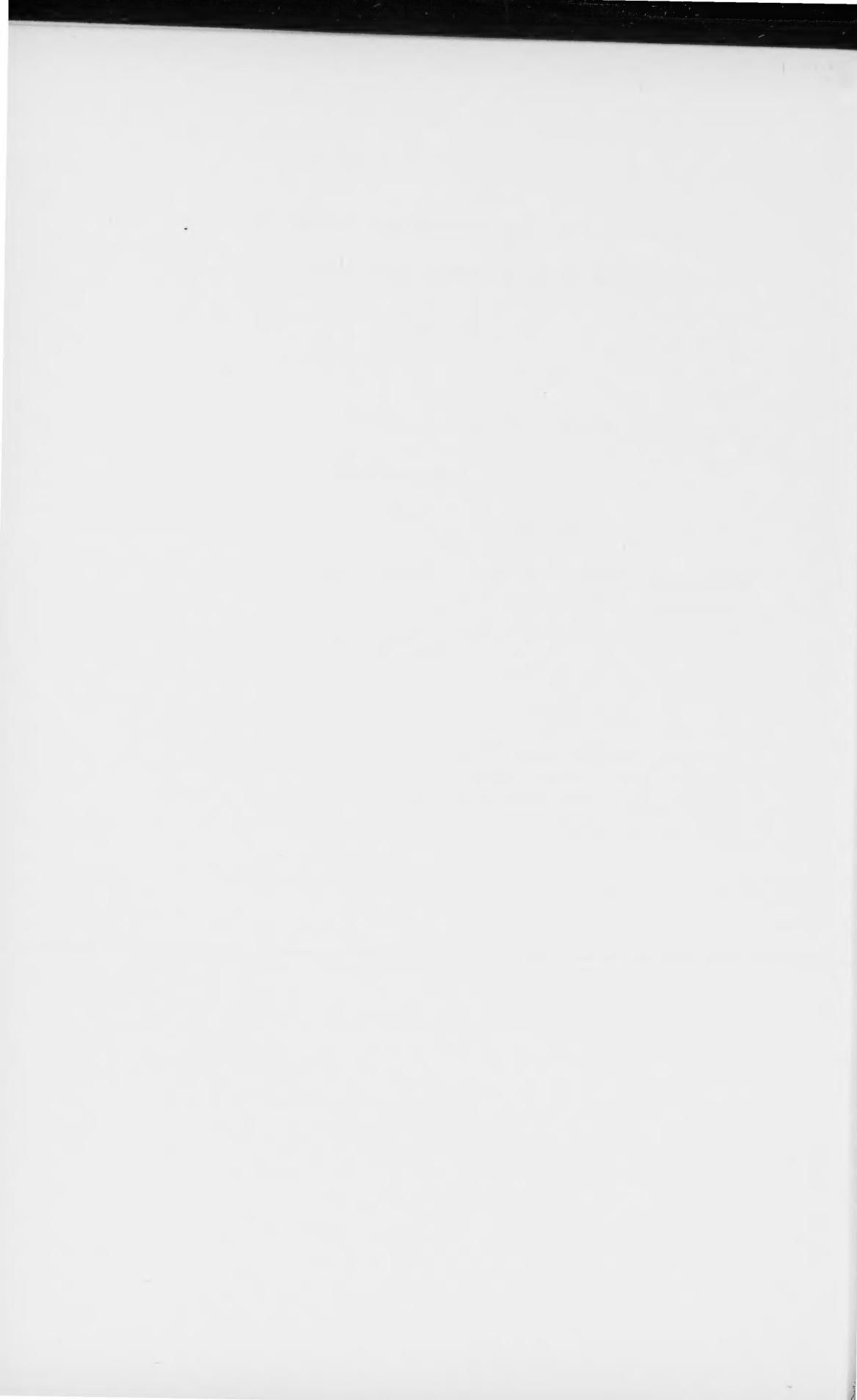
versus

Troxler Hosiery Co., Inc., and Gerald S.
Schafer, Trustee

Appellants.

Appeal from the United States District
Court for the Middle District of North
Carolina, at Greensboro. Hiram H. Ward,
District Judge

Upon consideration of the
appellants' petition for rehearing,



IT IS ORDERED that the petition for rehearing is denied.

Entered at the direction of Judge Chapman for a panel consisting of Chief Judge Winter, Judge Widener and Judge Chapman.

For the Court,

/s/ JOHN M. GREACEN
CLERK



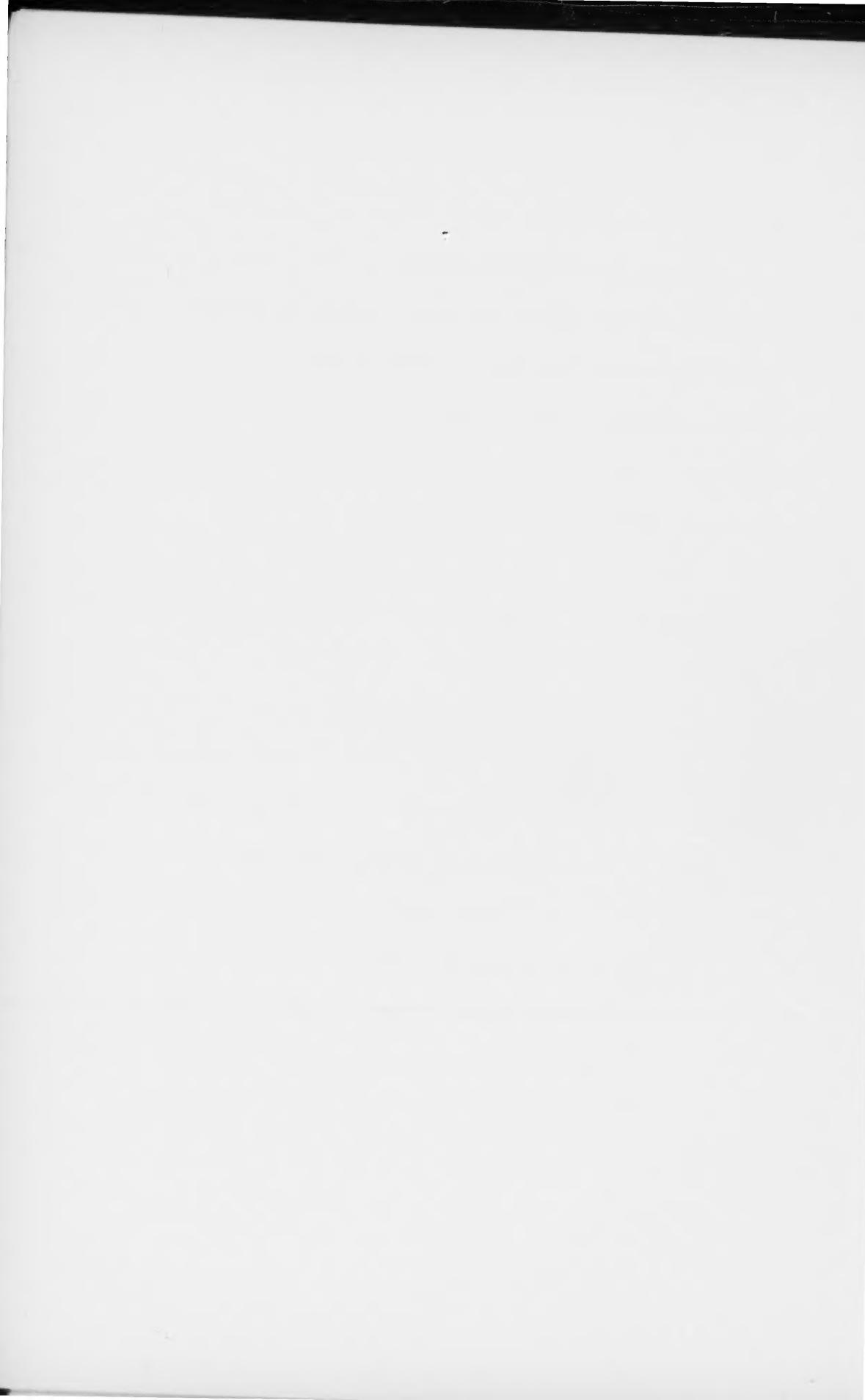
11 U.S.C. § 109.

(a) Notwithstanding any other provision of this section, only a person that resides or has a domicile, a place of business, or property in the United States, or a municipality, may be a debtor under this title.

(b) A person may be a debtor under chapter 7 of this title only if such a person is not -

(1) a railroad;

(2) a domestic insurance company, bank, savings bank, cooperative bank, savings and loan association, homestead association, credit union, or industrial bank or similar institution which is an insured bank as defined in

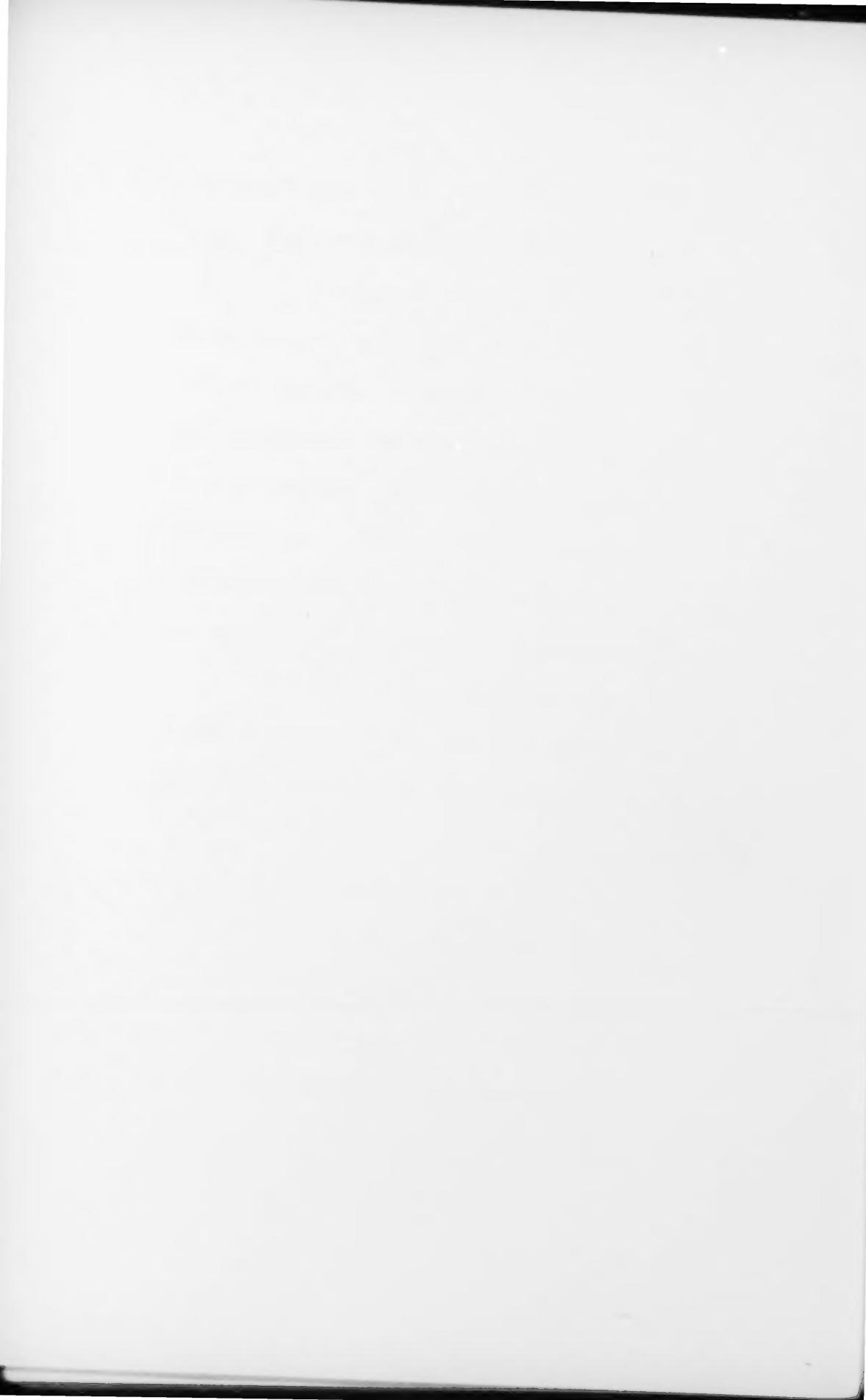


section 3(h) of the Federal Deposit Insurance Act (12 U.S.C. 1813(h)); or

(3) a foreign insurance company, bank, savings bank, cooperative bank, savings and loan association, building and loan association, homestead association, or credit union, engaged in such business in the United States.

(c) An entity may be a debtor under chapter 9 of this title if and only if such entity -

(1) is a municipality;
(2) is generally authorized to be a debtor under such chapter by State law, or by a governmental officer or



organization empowered by State law to authorize such entity to be a debtor under such chapter;

(3) is insolvent or unable to meet such entity's debts as such debts mature;

(4) desires to effect a plan to adjust such debts; and

(5) (A) has obtained the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter'

(B) has negotiated in good faith with creditors and has failed to obtain the agreement



of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;

(C) is unable to negotiate with creditors because such negotiation is impracticable or;

(D) reasonably believes that a creditor may attempt to obtain a transfer that is avoidable under section 547 of this title.

(d) Only a person that may be a debtor under chapter 7 of this title, except a stockbroker or a commodity broker, and a railroad may be a debtor

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under chapter 11 of this title.

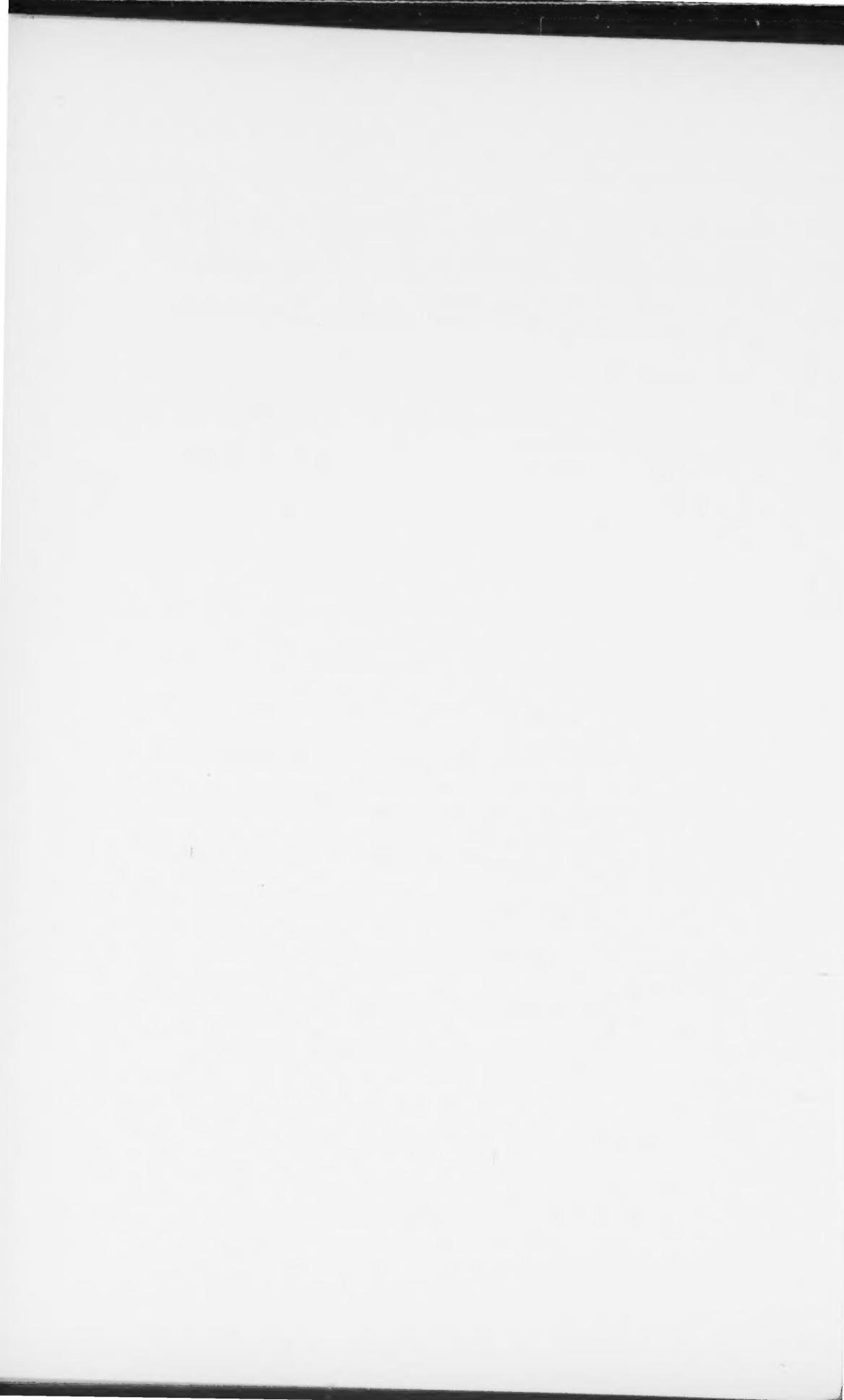
(e) Only an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than \$100,000 and noncontingent, liquidated, secured debts of less than \$350,000, or an individual with regular income and such individual's spouse, except a stock broker or a commodity broker, that owe, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts that aggregate less than \$100,000 and noncontingent, liquidated, secured debts of less than \$350,000 may be a debtor under chapter 13 of this title.

(f) Notwithstanding any other provision of this section, no individual



may be a debtor under this title who has been a debtor in a case pending under this title at any time in the preceding 180 days if -

- (1) the case was dismissed by the court for willful failure of the debtor to abide by orders of the court, or to appear before the court in proper prosecution of the case; or
- (2) the debtor requested and obtained the voluntary dismissal of the case following the filing of a request for relief from the automatic stay provided by section 362 of this title.



(11 U.S.C. § 362)

(a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970 (15 U.S.C. 78(a)(3)), operates as a stay, applicable to all entities, of-(1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;



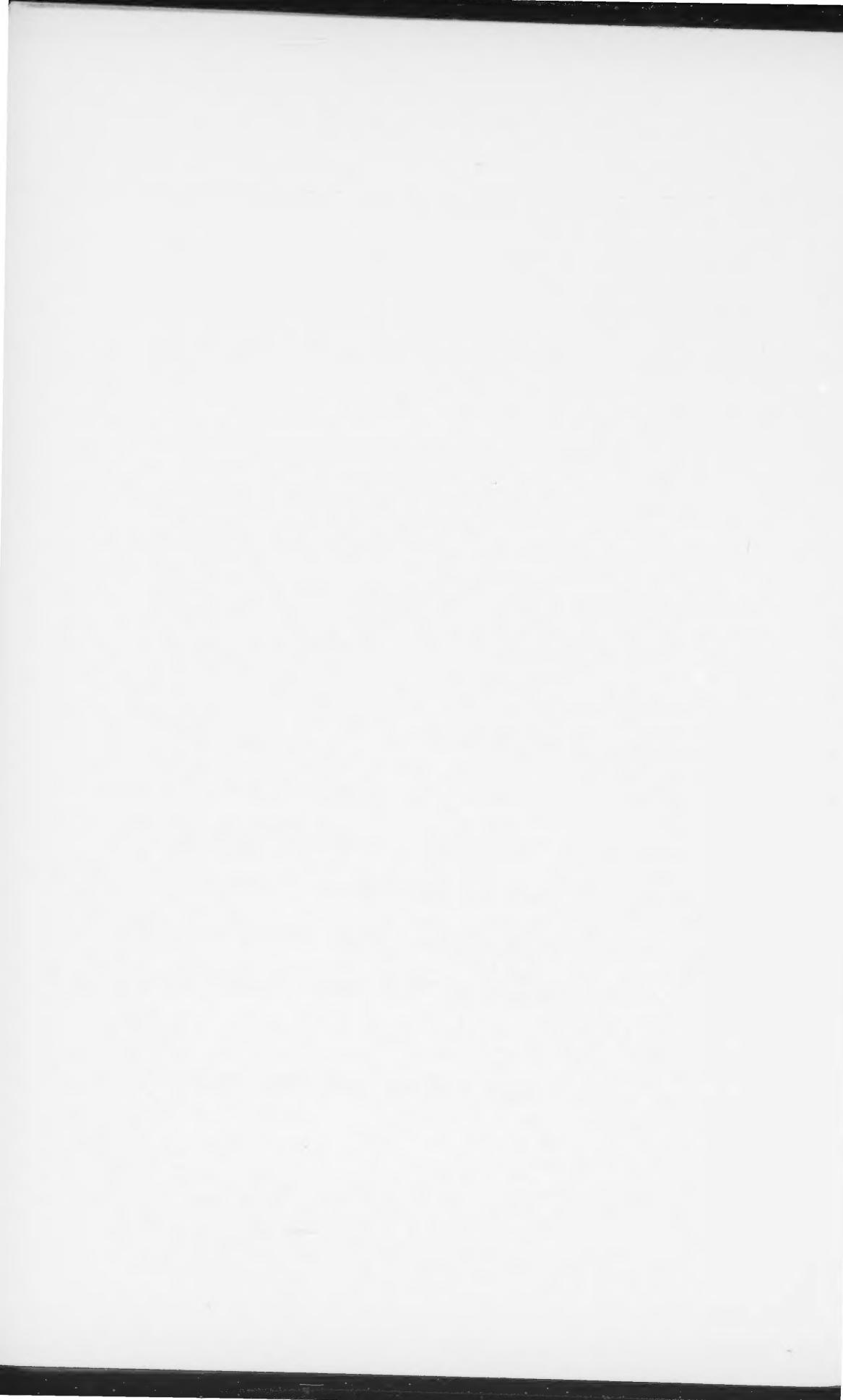
(2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;

(3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;

(4) any act to create, perfect, or enforce any lien against property of the estate;

(5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;

(6) any act to collect, assess,



or recover a claim against the debtor that arose before the commencement of the case under this title;

(7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and

(8) the commencement or continuation of a proceeding before the United States Tax Court concerning the debtor.

(b) The filing of a petition under section 301, 302, or 303 of this title, or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970 (15 U.S.C. 78(a)(3)), does not operate as a stay -

(1) under subsection (a) of this



section, of the commencement or continuation of a criminal action or proceeding against the debtor;

(2) under subsection (a) of this section, of the collection of alimony, maintenance, or support from property that is not property of the estate;

(3) under subsection (a) of this section, of any act to perfect an interest in property to the extent that the trustee's rights and powers are subject to such perfection under section 546(b) of this title or to the extent that such act is accomplished within the period provided under section 547(e)(2)(A) of this title;

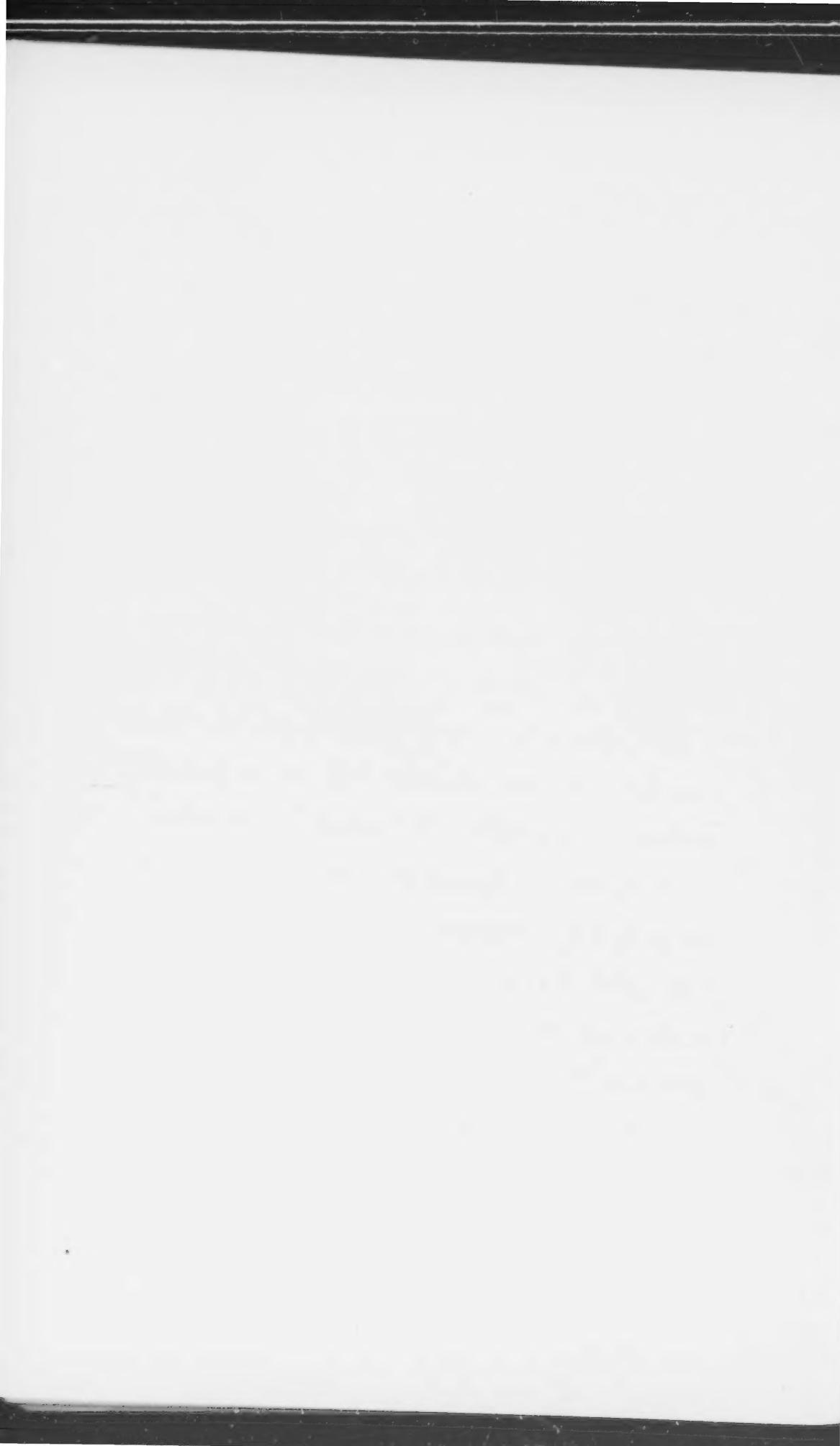
(4) under subsection (a)(1) of this section, of the commencement or continuation of an action or proceeding



by a governmental unit to enforce such governmental unit's police or regulatory power;

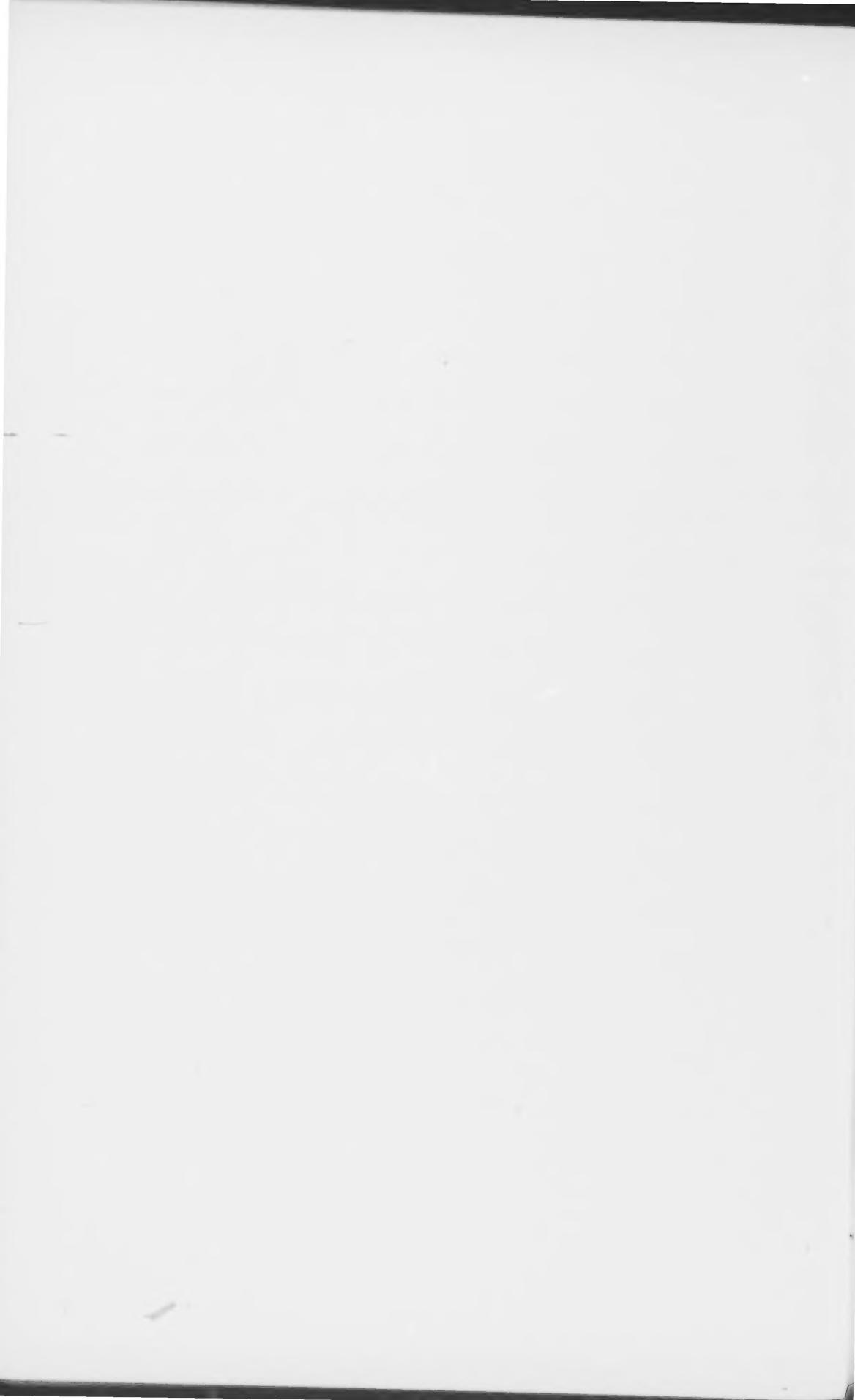
(5) under subsection (a)(2) of this section, of the enforcement of a judgment, other than a money judgment obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power;

(6) under subsection (a) of this section, of the setoff by a commodity broker, forward contract merchant, stockbroker, financial institution, or securities clearing agency of any mutual debt and claim under or in connection with commodity contracts, as defined in section 761(4) of this title, forward contracts, or securities contracts, as



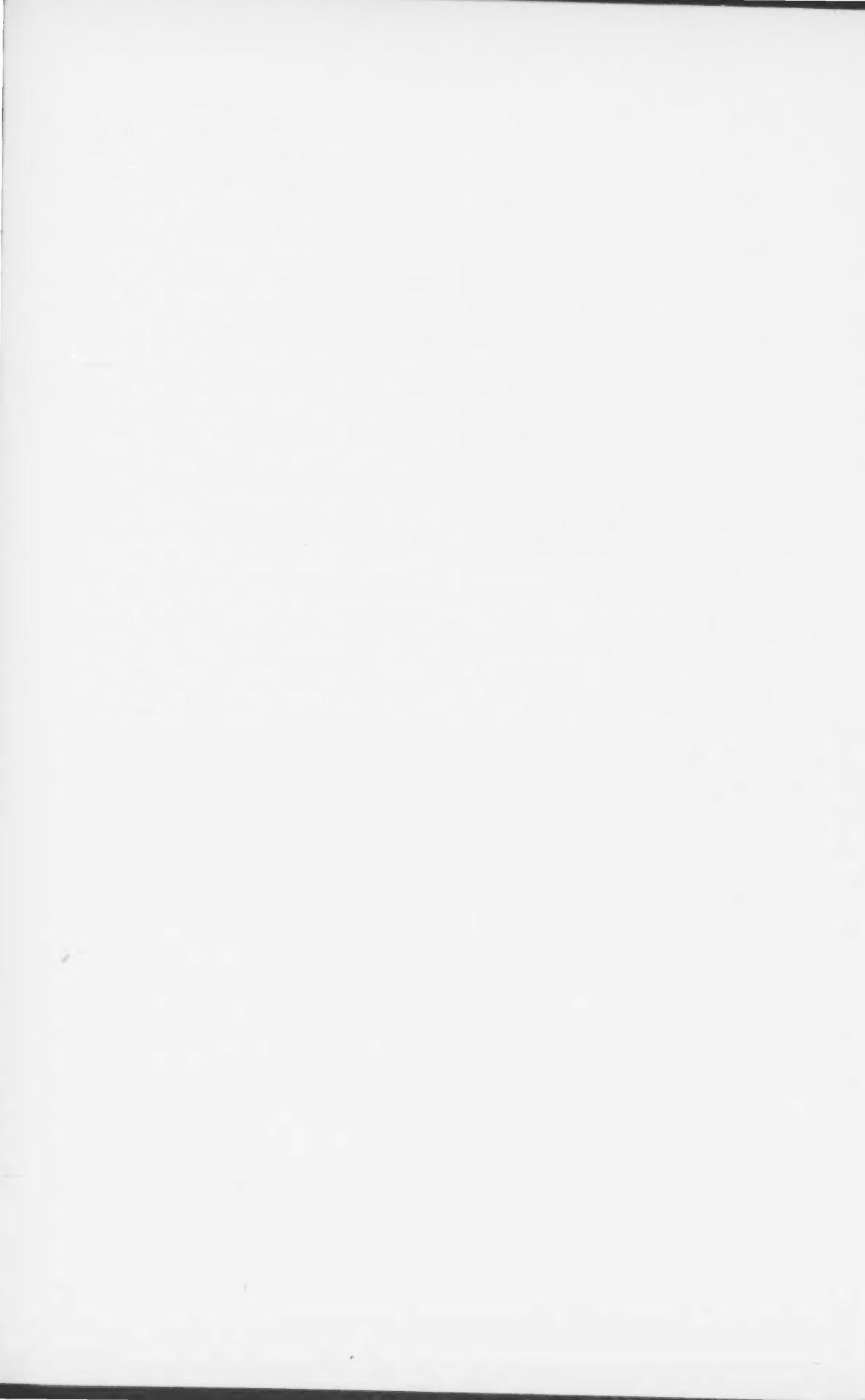
defined in section 741(7) of this title, that constitutes the setoff of a claim against the debtor for a margin payment, as defined in Section 741(5) or 761(16) of this title; or settlement payment, as defined in section 741(8) of this title, arising out of commodity contracts, forward contracts, or securities contracts against cash, securities, or other property held by or due from such commodity broker, forward contract merchant, stockbroker, financial institution, or securities clearing agency to margin, guarantee, secure, or settle commodity contracts, forward contracts, or securities contracts;

(7) under subsection (a) of this section, of the setoff by a repo participant, of any mutual debt and



claim under or in connection with repurchase agreements that constitute the setoff of a claim against the debtor for a margin payment, as defined in section 741(5) or 761(15) of this title, or settlement payment, as defined in section 741(8) of this title, arising out of repurchase agreements against cash, securities, or other property held by or due from such repo participant to margin, guarantee, secure or settle repurchase agreements;

(8) under subsection (a) of this section, of the commencement of any action by the Secretary of Housing and Urban Development to foreclose a mortgage or deed of trust in any case in which the mortgage or deed of trust held by the Secretary is insured or was

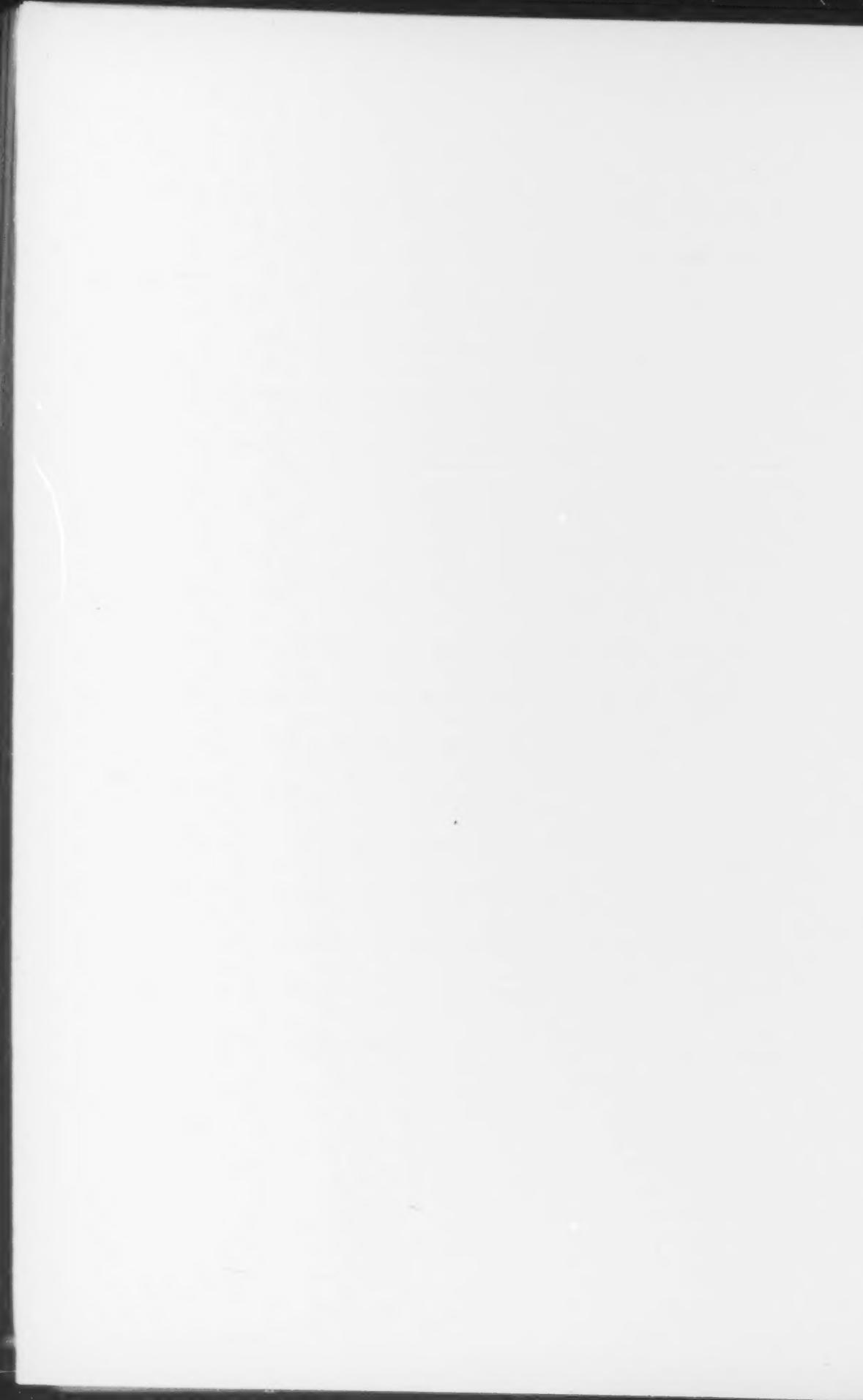


formerly insured under the National Housing Act and covers property, or combinations of property, consisting of five or more living units;

(9) under subsection (a) of this section, of the issuance to the debtor by a governmental unit of a notice of tax deficiency;

(10) under subsection (a) of this section, of any act by a lessor to the debtor under a lease of nonresidential real property that has terminated by the expiration of the stated term of the lease before the commencement of or during a case of this title to obtain possession of such property; or

(11) under subsection (a) of this section, of the presentment of a negotiable instrument and the giving of



notice of and protesting dishonor of such an instrument.

(c) Except as provided in subsections (d), (e), and (f) of this section -

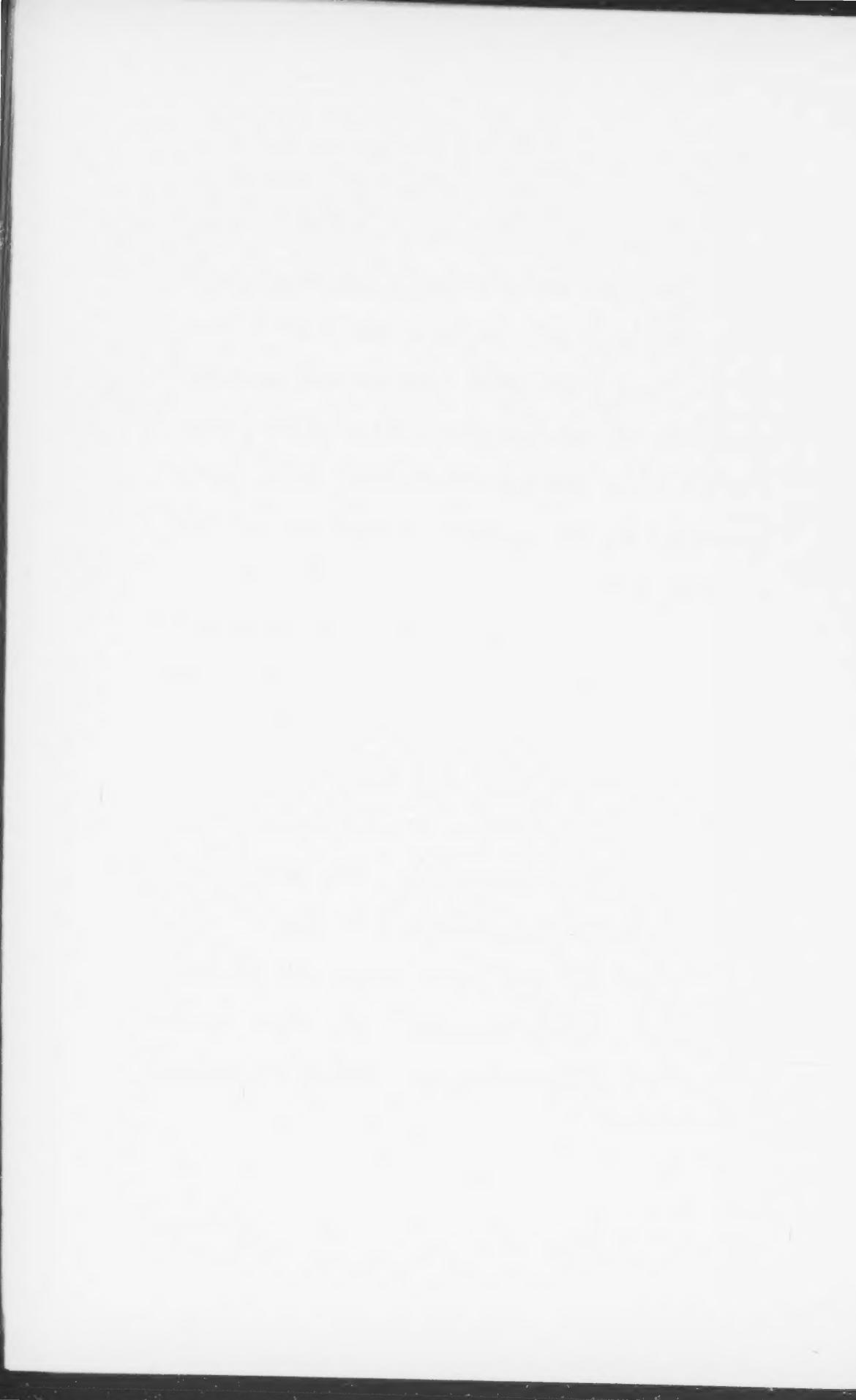
(1) the stay of an act against property of the estate under subsection (a) of this section continues until such property is no longer property of the estate; and

(2) the stay of any other act under subsection (a) of this section continues until the earliest of -

(A) the time the case is closed;

(B) the time the case is dismissed; or

(C) if the case is a case under Chapter 7 of this title concerning an individual or a



case under Chapter 9, 11, or 13 of this title, the time a discharge is granted or denied.

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay -

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest; or

(2) with respect to a stay of an act against property under subsection (a) of this section, if -

(A) the debtor does not have



equity in such property; and

(B) such property is not necessary to an effective reorganization.

(e) Thirty days after a request under subsection (d) of this section for relief from the stay of any act against property of the estate under subsection (a) of this section, such stay is terminated with respect to the party in interest making such request, unless the court, after notice and a hearing, orders such stay continued in effect pending the conclusion of, or as a result of, a final hearing and determination under subsection (d) of this section. A hearing under this subsection may be a preliminary hearing, or may be consolidated with the final



hearing under subsection (d) of this section. The court shall order such stay continued in effect pending the conclusion of the final hearing under subsection (d) of this section if there is a reasonable likelihood that the party opposing relief from such stay will prevail at the conclusion of such final hearing. If the hearing under this subsection is a preliminary hearing, then such final hearing shall be commenced not later than thirty days after the conclusion of such preliminary hearing.

(f) Upon request of a party in interest, the court, with or without a hearing, shall grant such relief from the stay provided under subsection (a) of this section as is necessary to

a

prevent irreparable damage to the interest of an entity in property, if such interest will suffer such damage before there is an opportunity for notice and a hearing under subsection (d) or (e) of this section.

(g) In any hearing under subsection (d) or (e) of this section concerning relief from the stay of any act under subsection (a) of this section -

(1) the party requesting such relief has the burden of proof on the issue of the debtor's equity in property; and

(2) the party opposing such relief has the burden of proof on all other issues.

(h) An individual injured by any willful violation of a stay provided by

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this section shall recover actual damages, including costs and attorneys' fees, and, in appropriate circumstances, may recover punitive damages.



11 U.S.C. § 541

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is compromised of all of the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

(2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case



that is -

(A) under the sole, equal, or joint management and control of the debtor; or

(B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.

(4) Any interest in property



preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date -

(A) by bequest, devise, or inheritance;

(B) as a result of the property settlement agreement with the



debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7) Any interest in property that the estate acquires after the commencement of the case.

(b) Property of the estate does not include -

- (1) any power that the debtor may exercise solely for the benefit of an entity other than the debtor; or
- (2) any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease before the commencement of the case under this title, and cases to include any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease during the case.

(c)(1) Except as provided in paragraph (2) of this subsection, an interest of the debtor in property becomes property of the estate under subsection (a)(1), (a)(2), or (a)(5) of this section notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law -

(A) that restricts or conditions transfer of such interest by the debtor; or

(B) that is conditioned on the insolvency or financial condition of the debtor, on the



commencement of a case under this title, or on the appointment of or taking possession by a trustee in a case under this title or a custodian before such commencement, and that effects or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in property.

(2) A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case

under this title.

(d) Property which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such mortgage, sold by the debtor but as to which the debtor retains legal title to service or supervise the servicing of such mortgage or interest, becomes property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.

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No. 86-1015

Supreme Court, U.S.
FILED

MAR 4 1987

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CLERK

In the Supreme Court of the United States

OCTOBER TERM, 1986

TROXLER HOSIERY CO. AND
GERALD S. SCHAFER, TRUSTEE, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS FOR
THE FOURTH CIRCUIT

BRIEF FOR THE UNITED STATES
IN OPPOSITION

CHARLES FRIED
Solicitor General

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QUESTIONS PRESENTED

1. Whether the district court and the court of appeals correctly held that 11 U.S.C. 362(b)(1), which provides that the filing of a bankruptcy petition does not stay "the commencement or continuation of a criminal action or proceeding against the debtor," authorizes the government to collect a criminal contempt fine notwithstanding the debtor's filing in bankruptcy.
2. Whether two circuit judges who sat on the panel that imposed the criminal contempt fine at issue should have recused themselves from the panel that heard the appeal on the question whether Section 362(b)(1) authorizes the government to collect the fine.

(I)



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**BRIEF FOR THE UNITED STATES
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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. C1-C4) is published at 796 F.2d 723. The opinion of the district court (Pet. App. B1-B29) is published at 41 Bankr. Rep. 457. The opinion of the bankruptcy court (Pet. App. A1-A7) is unpublished.

JURISDICTION

The judgment of the court of appeals was entered on August 4, 1986. A petition for rehearing was denied on September 24, 1986. The petition for a writ of certiorari was filed on December 20, 1986. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

The United States commenced forfeiture proceedings against hazardous sleepwear garments possessed by petitioner Troxler Hosiery Company in 1978. A district court ordered Troxler not to release the goods in question for sale in foreign commerce, and the court of appeals affirmed that order. Troxler nevertheless sold the goods. Troxler was subsequently found to be in criminal contempt for violating an order of the Fourth Circuit. It was fined \$80,000 plus costs and given 12 months from the date of judgment in August 1982 to pay the fine. Pet. App. B3-B6.

Troxler filed a reorganization petition under Chapter 11 of the Bankruptcy Code in November 1982.¹ The United States filed a proof of claim in the bankruptcy court, claiming a secured debt in the amount of \$82,733.48 on account of the fine and costs. The United States also sought a declaratory judgment that the automatic stay provisions of 11 U.S.C. 362(a) did not prevent it from collecting this amount. The bankruptcy court denied the government's request (Pet. App. A6-A7).

The district court reversed (Pet. App. B1-B30). It relied on 11 U.S.C. 362(b)(1), which provides that "[t]he filing of a petition [in bankruptcy] * * * does not operate as a stay * * * under subsection (a) of this section, of the commencement or continuation of a criminal action or proceeding against the debtor." The court noted that it was undisputed that the contempt proceedings against Troxler were criminal proceedings (*id.* at B12). It rejected petitioners' contention that Section 362(b)(1) permits the government to go forward with criminal proceedings but does not permit it to collect criminal fines. The court concluded that

¹The proceeding was converted to a liquidation proceeding under Chapter 7 in March 1984 (Pet. App. B7).

“[a]ction by the government to enforce the terms of a sentence are plainly a continuation of the entire criminal proceeding” (Pet. App. B13).

The court of appeals, in a per curiam opinion, adopted and affirmed the decision of the district court (Pet. App. C1-C4). Petitioners sought rehearing, challenging among other things the impartiality of two of the judges on the panel on the ground that those judges had sat on the panel that imposed the criminal contempt judgment (Pet. 12). Petitioners’ request for rehearing was denied (Pet. App. D1-D2).

ARGUMENT

1. The court of appeals’ decision that criminal proceedings are not stayed by the filing of a bankruptcy petition is correct. Petitioners do not allege a conflict among the circuits on that issue, and no conflict in fact exists. Accordingly, further review is unwarranted.

Subject to certain exceptions, 11 U.S.C. 362(a) stays claims against the debtor in bankruptcy proceedings.² Petitioners do not contest that the government may pursue criminal prosecutions against debtors, including prosecutions for criminal contempt, despite Section 362(a). Petitioners also seem to agree (see Pet. App. B13-B14) that, if a criminal prosecution produces a conviction, the government may enforce the terms of the sentence despite Section 362(a), provided that the sentence takes the form of a prison

²Section 362(a)(1) stays “the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title.” Section 362(a)(2) stays “the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case.”

term. However, petitioners assert that Section 362(a) stays the government's efforts to enforce the terms of a sentence for criminal contempt where the sentence takes the form of a fine.

But as the district court, affirmed by the court of appeals, concluded, 11 U.S.C. 362(b)(1) unambiguously excepts from the stay provision any "criminal action or proceeding," and the collection of a criminal fine is clearly part of a criminal action. As the district court stated (Pet. App. B12), "[s]entencing of a criminal defendant, whether it be imprisonment or imposition of a fine, fixes and declares the legal consequences of predetermined guilt." A criminal sentence "would be meaningless" if the government lacked power to enforce it, and actions by the government to enforce the terms of a sentence thus "are plainly a continuation of the entire criminal proceeding" (*id.* at B13).

If Congress had meant to provide that the government could go forward with criminal prosecutions against debtors in bankruptcy, but could not collect criminal penalties from them, it could easily have drafted the statute to accomplish that result. Congress could have provided in Section 362(b)(1) that Section 362(a)(1), which stays the commencement or continuation of actions, does not apply in criminal cases, but that Section 362(a)(2), which stays enforcement of judgments, does apply in criminal cases.³ But Congress did not draft the statute in that fashion. Instead, it provided in Section 362(b)(1) that a debtor's filing in bankruptcy does not operate as a stay, "*under subsection a of this section*, of the commencement or continuation of a criminal action or proceeding" (emphasis

³In other subsections of Section 362(b), Congress provided that exceptions to the stay provisions are applicable to certain subsections of Section 362(a) but not to others (see Section 362(b)(4) and (5)).

added). Congress thus evidenced its intent that *none* of the stay provisions of Section 362(a)—neither those applying to the commencement of actions nor those applying to the enforcement of judgments—apply in criminal cases. Accordingly, it is clear that Congress meant to permit criminal actions, including actions to enforce criminal penalties, to proceed despite the stay provisions of Section 362(a).

Petitioners also contend that while Section 362(b)(1) may authorize the commencement or continuation of a criminal action “against the debtor” despite the stay provisions of Section 362(a), it “does not apply to actions taken against ‘property of the estate’ ” (Pet. 21). Section 362(b)(1), of course, does speak of a criminal action or proceeding “against the debtor,” since criminal actions are typically commenced against persons rather than against property. As the district court concluded, however, this language “is broad enough to include enforcement of a judgment through pecuniary collection means” from the debtor *or* his property, since enforcement of the sentence is the final step in a criminal action against the debtor himself (Pet. App. B14). As noted above, Section 362(a)(2) generally does prevent “the enforcement, against the debtor *or against property of the estate*, of a judgment obtained before the commencement” of bankruptcy; if Congress had wished to foreclose the enforcement of criminal fines against property of the estate, it could easily have drafted the Section 362(b)(1) exception accordingly. As we have explained, however, Congress did not do so, but rather provided that *none* of the stays described in Section 362(a) is applicable to criminal proceedings.⁴

⁴The cases cited by petitioners (Pet. 22) are not to the contrary. In neither *In re Nashville White Trucks, Inc.*, 731 F.2d 376 (6th Cir. 1984), nor *Matter of Gibbs*, 9 Bankr. Rep. 758 (Bankr. D. Conn. 1981), did the court mention Section 362(b)(1), since those cases did not involve criminal proceedings. In *In re Ryan*, 15 Bankr. Rep. 514, 518-519 (Bankr. D. Md. 1981), the court held that Section 362(b)(1) did not apply, but it did so because it concluded that the forfeiture proceeding at issue was not a criminal proceeding.

Petitioners assert that the result reached by the courts below conflicts with the Bankruptcy Code by giving the government a super-priority position compared to other creditors, contrary to the statutory priority scheme (Pet. 22-23). This assertion is incorrect, since Congress plainly provided in Section 362(b)(1) that the government may enforce criminal sentences despite the automatic stay provisions, thus indicating that the government need not file claims like other creditors (and be subject to the priority rules) in order to collect criminal fines. The district court recognized that its holding placed the government in a superior position to Troxler's unsecured creditors, but concluded that "[a] sovereign's interest in protecting its citizens through the criminal law is fundamentally different from private financial concerns and for that reason must take precedence" (Pet. App. B24-B25). That holding is congruent with this Court's recent holding in *Kelly v. Robinson*, No. 85-1033 (Nov. 12, 1986), that restitution obligations imposed as part of a criminal sentence are not dischargeable in bankruptcy.

2. Petitioners' other contention, that the two circuit judges who sat on the panel that imposed the criminal contempt fine should have recused themselves from hearing the appeal on the stay question, is plainly without merit. Federal law provides for disqualification "in any proceeding in which [a judge's] impartiality might reasonably be questioned." 28 U.S.C. 455(a). But Section 455(a) does not require disqualification merely because a judge has been involved in prior judicial proceedings involving the same matter or party. See *United States v. Studley*, 783 F.2d 934, 939 (9th Cir. 1986) ("a judge's prior adverse ruling is not sufficient cause for recusal"). It is well established that the prejudice to which Section 455(a) is addressed is bias stemming from an "extra-judicial source." *In re Manoa Finance Co.*, 781 F.2d 1370, 1373 (9th Cir. 1986) (citing cases). There

is no allegation of extra-judicial prejudice here. Rather, the source of the prejudice hypothesized by petitioners is the judges' prior participation in *judicial* proceedings involving Troxler. Moreover, the appeal on the bankruptcy stay issue presented a question of statutory construction wholly unrelated to the propriety of the criminal contempt judgment. There is thus no reason to think that the judges who decided the bankruptcy law issue were influenced in any way by their prior decision.⁵

CONCLUSION

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

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MARCH 1987

⁵It apparently did not occur to petitioners until after the court had rendered its decision that the judges considering the bankruptcy question should have disqualified themselves, since petitioners raised the disqualification issue for the first time in their rehearing petition. Even if there were merit to petitioners' claim that the judges should have recused themselves, petitioners should have raised their objection earlier and should be deemed to have waived it by not raising it in a timely fashion. Allowing them to raise the objection after the panel issued its decision would give them two chances at obtaining reversal by the court of appeals and encourage other litigants to wait before raising claims under Section 455(a).